

The Global Economy

UNIT PACING CHART

	Chapter 16	Chapter 17	Chapter 18
Day 1	Unit Opener Chapter Opener Section 1	Chapter Opener Section 1	Chapter Opener Section 1
Day 2	Case Study Section 2 BusinessWeek Newsclip	Case Study Section 2 BusinessWeek Newsclip	BusinessWeek Newsclip Section 2 Case Study
Day 3	Section 3 Profiles in Economics	Section 3 Profiles in Economics	Section 3 Profiles in Economics
Day 4	Review Chapter Assessment	Review Chapter Assessment	Review Chapter Assessment
Day 5	Debates in Economics		The Global Economy & You



Teacher to Teacher



Jay Grenawalt
George
Washington High
School
Denver, Colorado

Foreign Investment Increasingly, new factories are being constructed outside of national boundaries. In such an environment, nations will have to compete for foreign companies just as U.S. cities and states do today. **Ask:** *What factors might lead a firm to build a factory in Country A instead of Country B?* (Some factors that might provide incentives/disincentives include wages, skilled labor, political stability, transportation and communication systems, import-export restrictions, government regulations, cultural and linguistics factors, and the size of the foreign country's market.)

Present students with a hypothetical situation. Suppose a company wants to build an automobile plant. Organize students into groups and ask each group to pick five nations that represent a diversity of development and regions. Using current encyclopedias, the *World Development Report*, *The Index of Economic Freedom*, and magazine and newspaper articles, have groups compile brief overviews of each economy using the previous criteria. The students in each group should discuss and reach a consensus about which country would be their choice for the plant. As a class, tabulate the votes of the groups and lead a discussion about the choices.

Author Note



Dear Economics Teacher:

Just a few years ago, any textbook that wanted to talk about the global economy would only have to mention the opening of a new McDonald's in Moscow or speculate about the impact of the rising number of low-cost Japanese cars that were beginning to compete with the so-called "big three" automakers in Detroit. Some of the big issues of today, such as offshoring, globalization, and global warming, were not even part of our everyday vocabulary. How things have changed!

On balance, they have changed for the better. Consumers have more choices than ever, and the flood of low-priced products from abroad has helped to keep prices down. While some jobs have gone abroad, economists generally agree that we are better off now than we were 20 years ago.

When I think about the global economic changes in the last 20 years, I am reminded of our earlier discussion of voluntary exchange, exchange that takes place only because each party feels better off after the transaction than before. A lot of exchanges occurred on the way to globalization, and so a lot of people must have felt that the changes were beneficial to them. In short, globalization is happening because we want it and allow it to happen!

The rapid globalization dramatically validates our economic theories—in particular specialization, competition, comparative advantage, and the gains from trade. People sometimes wonder about the usefulness of abstract economic theories, but the current global economic changes show that the economist's view of why and how things happen is right on target! In fact, it is the global economy where real-world developments fall most neatly into the theoretical and methodological framework we covered in this text.

Making accurate predictions about the future is part of why economics is so useful and fun. It's also been fun authoring this book. I hope that using it has been fun for you and your students as well!

A handwritten signature in dark ink that reads "Gary E. Clayton". The signature is fluid and cursive, with a long horizontal line extending from the end.

Gary Clayton, Ph.D.
Author

Unit Objectives

After studying this unit, students will be able to:

- **Recognize** the importance of international trade, foreign exchange, and the interdependence among nations.
- **Analyze** the problems of economically developing countries.
- **Describe** significant global challenges.

Unit Overview

Unit 5 examines economics from a global perspective.

Chapter 16 examines absolute and comparative advantage, barriers to international trade, and foreign exchange and trade deficits.

Chapter 17 discusses the problems faced by developing countries, including countries moving toward more capitalistic economic systems.

Chapter 18 reviews the economic challenges that the world faces and the use of economics in analyzing choices and making decisions.

CHAPTER 16

International Trade

CHAPTER 17

Developing Countries

CHAPTER 18

Global Economic Challenges

This Japanese-owned Honda manufacturing plant in Marysville, Ohio, reflects increasingly global markets and production.



438 UNIT 5

Activity: Launching the Unit

International Trade Have the class role-play a congressional subcommittee meeting on a plan to raise tariffs on imported products—athletic shoes, for example. Select several students to act as subcommittee members and four or five others to act as witnesses—consumer advocates, workers in the shoe-making industry, executives from American shoe manufacturers, and executives

from foreign shoe manufacturers. Encourage expert witnesses to make presentations to the subcommittee for or against the raise in tariffs, and have subcommittee members ask them questions. Have the rest of the class act as reporters and write summaries of the procedures. **OL**



INTRODUCING UNIT 5

Making It Relevant

Provide students with copies of newspapers and current affairs magazines. Direct them to skim through these periodicals to locate advertisements for foreign goods. Encourage students to ask themselves the following questions about the advertisements: **What good is advertised? Where is it made? How was it transported to the United States? Do American companies make this good? If so, why do you think we buy it from other countries?**

Have students discuss their answers. Conclude by pointing out that the chapters in this unit deal with such topics as international trade and the growing interconnectedness of the world's economies. **OL**

BusinessWeek **ONLINE**

To find up-to-date news and analysis on the economy, business, technology, markets, entrepreneurs, investments, and finance, have students search feature articles and special reports on the BusinessWeek Web site, www.businessweek.com.

Extra Credit Project

Have students research organizations such as the Ford Foundation, the International Finance Corporation (IFC), and agencies of the United Nations (UN) that offer loans or grants to economically developing nations. Have students write short reports with graphs

showing trends in assistance offered. Suggest that students combine their reports into a pamphlet titled *International Organizations and Economic Development*. **AL**



















16 Planning Guide

Key to Ability Levels

BL Below level	AL Above level
OL On level	ELL English Language Learners

Key to Teaching Resources

 Print Material	 DVD
 CD-Rom	 Transparency





































Levels				Resources		Chapter Opener	Section 1	Section 2	Section 3	Chapter Assess
BL	OL	AL	ELL							
FOCUS										
BL	OL	AL	ELL		Daily Focus Skills Transparencies		80	82	81	
TEACH										
BL	OL		ELL		Guided Reading Activities*		p. 46	p. 47	p. 48	
BL	OL	AL	ELL		Economic Content Vocabulary Activities*		p. 16	p. 16	p. 16	
	OL	AL			Critical Thinking Activities		p. 22	p. 22	p. 22	
BL	OL		ELL		Reading Essentials and Note-Taking Guide*		p. 136	p. 139	p. 142	
		AL			Enrichment Activities		p. 16			
	OL	AL			Free Enterprise Activities			p. 22		
BL	OL	AL	ELL		Primary and Secondary Source Readings			p. 43		
BL	OL	AL	ELL		Hands-On Economics				p. 24	
BL	OL	AL	ELL		Economic Concepts Transparencies, Strategies, and Activities		p. 39		p. 41	
BL	OL	AL	ELL		Math Practice for Economics				p. 22	
BL	OL	AL	ELL		Economics Forms and Financial Pages Transparencies, Strategies, and Activities		p. 11		p. 26	
	OL	AL			BusinessWeek Focus on the Global Economy			pp. 2, 10, 17	p. 25	
BL	OL	AL	ELL		Reinforcing Economic Skills		p. 26		p. 20	
BL	OL		ELL		High School Reading in the Content Area Strategies and Activities	✓	✓	✓	✓	✓
BL	OL	AL	ELL		High School Writing Process Transparencies	✓	✓	✓	✓	✓
BL	OL	AL	ELL		Writer’s Guidebook	✓	✓	✓	✓	✓
BL	OL	AL	ELL		StudentWorks Plus CD-ROM	✓	✓	✓	✓	✓
BL	OL	AL	ELL		Vocabulary PuzzleMaker CD-ROM	✓	✓	✓	✓	✓

*Also available in Spanish



- Interactive Lesson Planner
- Interactive Teacher Edition
- Fully editable blackline masters
- Economics & You videos

- Differentiated Lesson Plans
- Printable reports of daily assignments
- Standards tracking system

Levels				Resources		Chapter Opener	Section 1	Section 2	Section 3	Chapter Assess
BL	OL	AL	ELL							
TEACH <i>(continued)</i>										
BL	OL	AL	ELL		Economics & You Video Program DVD— <i>International Trade</i>					
BL	OL	AL	ELL		Graph Coach CD-ROM					
Teacher Resources					Differentiated Instruction Strategies					
					Success with English Learners					
					Presentation Plus! CD-ROM					
ASSESS										
BL	OL	AL	ELL		Section Quizzes and Chapter Tests		p. 201	p. 202	p. 203	pp. 205, 209
BL	OL	AL	ELL		Authentic Assessment Strategies and Activities		p. 22	p. 8	p. 25	
BL	OL	AL	ELL		ExamView® Assessment Suite CD-ROM		16-1	16-2	16-3	Ch. 16
BL	OL	AL	ELL		Interactive Tutor Self-Assessment CD-ROM		16-1	16-2	16-3	
CLOSE										
BL			ELL		Reteaching Activities*		p. 16	p. 16	p. 16	
BL	OL		ELL		Reading and Study Skills Foldables		pp. 63, 64	pp. 63, 64	pp. 63, 64	

*Also available in Spanish

Activity Using StudentWorks™ Plus

Daily Assignments and Grade Log

Technology Product

Glencoe's *StudentWorks™ Plus* CD-ROM contains everything your students need, including the complete Student Edition and access to all student workbooks. *StudentWorks™ Plus* also includes a Daily Assignment and Activity Log that allows students to

- record and track progress on their daily assignments and responsibilities;
- log results achieved, including their grades;
- sort assignments alphabetically or by category;
- view and print the assignment and grade log in a table or calendar format.

Objectives


Using *StudentWorks™ Plus* will help your students

- take responsibility for their individual tasks;
- improve independent study skills.

Steps

Provide students with the following information:

- Launch *StudentWorks™ Plus*.
- Select the **Daily Assignments and Grade Log** button at the bottom of the launch screen.
- Create a new file or open an existing one. The log is organized as a table, with a row of information for each assignment.
- Add information for each assignment, including the date of the assignment, the name, additional comments, the due date, and the grade.
- Edit rows as assignment information is provided or changed. Add a new row to the log for each new assignment.

			
	Student	Teacher	Parent
Beyond the Textbook	•	•	•
Chapter Overviews	•	•	•
ePuzzles and Games	•		•
Concepts in Motion	•		•
Multi-Language Glossaries	•		•
Online Student Edition	•	•	•
Self-Check Quizzes	•		•
Student Web Activities	•		•
Study Central™	•		•
Time Current Events	•	•	•
Teaching Today		•	
Vocabulary eFlashcards	•		•
Web Activity Lesson Plans		•	



READING SUPPORT FROM JAMESTOWN EDUCATION

- **Timed Readings Plus in Social Studies** helps students increase their reading rate and fluency while maintaining comprehension. The 400-word passages are similar to those found on state and national assessments.
- **Reading in the Content Area: Social Studies** concentrates on six essential reading skills that help students better comprehend what they read. The book includes 75 high-interest nonfiction passages written at increasing levels of difficulty.
- **Reading Social Studies** includes strategic reading instruction and vocabulary support in Social Studies content for both ELLs and native speakers of English.
www.jamestowneducation.com

Reading List Generator CD-ROM

GLENCOE BOOKLINK 3

Use this database to search more than 30,000 titles to create a customized reading list for your students.

- Reading lists can be organized by students' reading level, author, genre, theme, or area of interest.
- The database provides Degrees of Reading Power™ (DRP) and Lexile™ readability scores for all selections.
- A brief summary of each selection is included.

Leveled reading suggestions for this chapter:

For students at a Grade 10 reading level:

- **India: A Study of an Economically Developing Country**, by David Cumming

For students at a Grade 11 reading level:

- **Voyaging to Cathay: Americans in the China Trade**, by Alfred Tamarin & Shirely Glubok

For students at a Grade 12 reading level:

- **Ghana: A Study of an Economically Developing Country**, by Steve Brace

* Review suggested books before assigning them.



National Council on Economic Education

Voluntary Standards Emphasized in Chapter 16

Content Standard 6 When individuals, regions, and nations specialize in what they can produce at the lowest cost and then trade with others, both production and consumption increase.

Content Standard 17 Costs of government policies sometimes exceed benefits. This may occur because of incentives facing voters, government officials, and government employees, because of actions by special interest groups that can impose costs on the general public, or because social goals other than economic efficiency are being pursued.

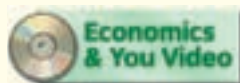
Resources Available from NCEE

- Virtual Economics®: An Interactive Center for Economic Education Version 3.0
- Civics and Government: Focus on Economics, Second Edition
- Advanced Placement Economics: Teacher Resource Manual, Third Edition
- Focus: Understanding Economics in U.S. History
- Focus: High School Economics, Second Edition
- Capstone: The Nation's High School Economics Course
- Focus: Institutions and Markets

To order these materials, or to contact your State Council on Economic Education about workshops and programs, call 1-800-338-1192 or visit the NCEE Web site at store.ncee.net.

The BIG Idea

As students study the chapter, remind them to consider the chapter-based Big Idea. The **Essential Question** in the chapter launch activity below ties in to the Big Idea and helps students think about and understand important chapter concepts. In addition, the Hands-On Chapter Project relates the content from each section to the Big Idea. The steps in each section build on each other and culminate in the Wrap-Up Activity on the Visual Summary page.



To generate student interest and

provide a springboard for class discussion, access the Economics & You Topic 23 video, **International Trade**, at glencoe.com or on the video DVD.



Dinah Zike's Foldables

are three-dimensional, interactive graphic organizers that help students practice basic writing skills, review key vocabulary terms, and identify main ideas. Have students complete this chapter's Foldable activity or activities in *Dinah Zike's Reading and Study Skills Foldables* booklet. **OL**

Economics ONLINE

Introduce students to chapter content and key terms by having them access **Chapter 16—Chapter Overviews** at glencoe.com.

Why It Matters

You and a classmate are planning to open a lawn-service business. You will each contribute \$200 toward the purchase of a mower, gas can, trimmer, and other materials for the business. Now it is time to get organized. Work with a classmate and make a list of the different “jobs” associated with your lawn-service business. What criteria will you use to divide up these jobs? Why? Read Chapter 16 to find out how nations make decisions about what to produce and trade with other nations.

The BIG Idea

Trade and specialization lead to economic growth for individuals, regions, and nations.

International trade allows us to purchase items produced in any country, such as the items from Africa and the Caribbean in a store in Syracuse, New York.

440 UNIT 5



Economics ONLINE Chapter Overview Visit the *Economics: Principles and Practices* Web site at glencoe.com and click on **Chapter 16—Chapter Overviews** to preview chapter information.

Activity: Launching the Chapter

Identifying Have students imagine that they are owners of a small manufacturing company. Tell them that they have an opportunity to increase sales of their products by exporting them. Ask students to identify the laws, customs, consumer preferences, and other types of information they would need to know about the countries to which they intend to export. Discuss their responses

as a class. **Essential Question:** **Why do governments encourage the businesses in their country to trade with other nations?** (*World trade strengthens a nation's economy by allowing a country to acquire needed goods and services while making efficient use of its own resources.*) **OL**

Absolute and Comparative Advantage

GUIDE TO READING

Section Preview

In this section, you will learn that comparative advantage is the basis for international trade.

Content Vocabulary

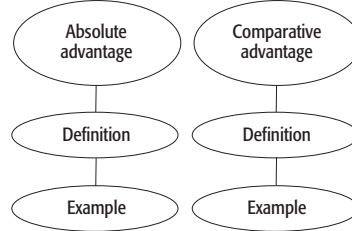
- exports (p. 442)
- imports (p. 442)
- absolute advantage (p. 443)
- production possibilities frontier (p. 444)
- comparative advantage (p. 444)
- opportunity cost (p. 444)

Academic Vocabulary

- volume (p. 443)
- enabled (p. 444)

Reading Strategy

Defining As you read the section, complete graphic organizers similar to the ones below by defining each term and providing an example of each.



ISSUES IN THE NEWS

—BusinessWeek

Russia: Shoppers Gone Wild

It's midday on Saturday, and the Mega-1 mall in southern Moscow is packed. Shoppers have come to stock up on groceries at the mall's French-owned Auchan hypermarket, buy furniture at Swedish retailer IKEA, and browse dozens of boutiques selling everything from Yves Rocher cosmetics to Calvin Klein underwear. Although crammed with expensive Western merchandise, Mega has been a hit since it opened its doors in December, 2002. Last year it was the world's most frequented shopping center, with 52 million visitors.

Down the road at the Rolf car dealership, Oxana Starostina is filling in registration forms for her new Mitsubishi Lancer, purchased with \$20,000 in cash. She and her husband, Maxim, saved the money from their small construction supply business.

... [F]or many multinationals from the U.S., Europe, and Asia, the consumer boom, not oil and gas, is the investment story to watch. ■



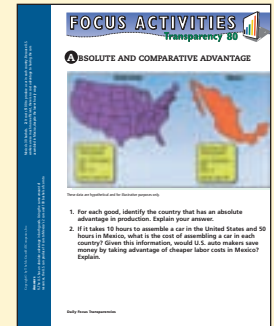
Nations trade for the same reasons that individuals do—because they believe that the products they receive are worth more than the products they give up. International trade is partially responsible for the incredible variety of goods and services both we and the shoppers in the news story consume.

For example, we purchase clothing made in China, oil from the Middle East, bananas from Honduras, and coffee beans from Colombia and Brazil. We consume a service when we vacation in the Caribbean or in Europe. The shoppers in Moscow are doing the same thing: enjoying the goods produced in France, Sweden, and Japan.

Focus

Bellringer

Daily Focus Transparency 80



GUIDE TO READING

Answers to Graphic:

Absolute advantage: country's ability to produce more of a given product than another country can produce. Examples will vary.

Comparative advantage: country's ability to produce a given product relatively more efficiently than another country by doing it at a lower opportunity cost. Examples will vary.

Resource Manager

R Reading Strategies

Teacher Edition

- Reading Graphs, p. 444
- Det. Importance, p. 445

Additional Resources

- Guid. Read. Act., p. 46
- Read. Ess. & Note-Taking Guide, p. 136

C Critical Thinking

Teacher Edition

- Analyzing, pp. 442, 446

Additional Resources

- Crit. Think. Act., p. 22
- Econ. Concepts Trans., Strat. and Act., p. 39
- Enrichment Act., p. 16

D Differentiated Instruction

Teacher Edition

- ELL, p. 443

Additional Resources

- Bus. Focus on the Global Economy, p. 2
- Econ. Forms and Fin. Pages Trans., Strat. and Act., p. 11

W Writing Support

Teacher Edition

- Expository Writing, p. 444

Additional Resources

- Writer's Guidebook
- Reading and Study Skills Fold., p. 63

S Skill Practice

Teacher Edition

- Using Charts and Tables, p. 442
- Visual Literacy, p. 443

Additional Resources

- Reinforcing Econ. Skills, p. 26
- Reteach. Act., p. 16

Teach

C Critical Thinking

Analyzing Ask: What is the relationship between a state or nation's exports and its specialization? (A state or nation's main exports show what the place produces and sells to other countries; this indicates that the state or nation has specialized in these goods.) Invite students to research exports produced in their state and then analyze why the state might specialize in these items. **AL**

S Skill Practice

Using Charts and Tables Ask: From which countries does the United States import tin? (Peru, China, Bolivia, Indonesia) What percent of U.S. tin consumption do these imports represent? (88 percent) **BL**

Economic Analysis

Answer: They must become interdependent with one another in order to acquire the raw materials they need.

Differentiated Instruction

exports the goods and services that a nation sells to other nations

imports the goods and services that a nation buys from other nations

Why Nations Trade

MAIN Idea Trade allows nations to specialize in some products and then trade them for goods and services that are more expensive to produce.

Economics and You When you were young, did you ever trade toys, cards, or candy with your friends? Read on to learn about international trade.

Some trade takes place because countries lack goods at home. **Figure 16.1** shows some essential raw materials used in the United States that come from abroad.

Specialization

A more important reason for trade—whether among people, states, or countries—is specialization. When people specialize, they produce the things they do best and exchange those products for the things that other people do best.

States also specialize. For example, New York is a financial center for stocks and bonds, while automobiles are a major industry in Michigan. Texas is known for oil and cattle, while Florida and California are famous for citrus fruit. Countries specialize in different goods and services in much the same way.

If you want to find out what a country specializes in, look at its **exports**—the goods and services that it produces and sells to other nations. If you want to see what a country would like to have but does not produce as efficiently, look at its **imports**—the goods and services that one country buys from other countries.

Extent of Trade

International trade is important to all nations, even a country as large as the United States. Most of the products that

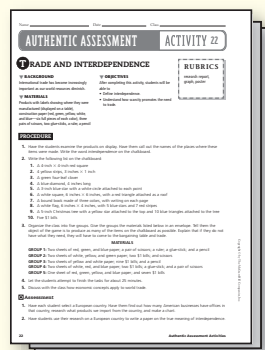
Figure 16.1 American Dependence on Trade

Raw Material	Imports as a Percent of Consumption	Primary Foreign Sources	Use of Raw Materials
Industrial diamonds	100	South Africa, Australia, Democratic Republic of the Congo, Botswana	Industrial cutting tools, oil well drills
Bauxite	100	Jamaica, Guinea, Brazil, Guyana	Anything made of aluminum
Columbium	100	Brazil, Canada, Thailand	Rocket structures and heat radiation shields
Mica (sheet)	100	India, Belgium, France	Electrical insulation, ceramics
Strontium	100	Mexico, Spain	Flares, fireworks
Tin	88	Peru, China, Bolivia, Indonesia	Cans and containers, electrical components
Tantalum	80	Thailand, Germany, Brazil	Surgical instruments, missile parts
Barite	79	China, India	Filler for gas and oil well drilling fluids, paint, plastics
Cobalt	76	Democratic Republic of the Congo, Zambia, Canada	High-temperature jet fighter engines
Chromium	72	South Africa, Zimbabwe, Turkey	Chrome, ball bearings, trim on appliances and cars

Sources: Statistical Abstract of the United States; U.S. Geological Survey

► International trade is the primary means by which nations, including the United States, obtain many essential materials.

Economic Analysis How does the lack of certain raw materials force nations to become more interdependent?



Authentic Assessment Strategies and Activities, p. 22

Trade and Interdependence

Objective: Define interdependence and understand how scarcity promotes trade.

Focus/Teach: Ask students why nations might trade with one another. Then have students complete the activity.

Assess: Have students use their charts and papers to make a presentation about interdependence.

Close: Have students explain which trade commodities the items used in the activity could represent.

Differentiated Instruction Strategies

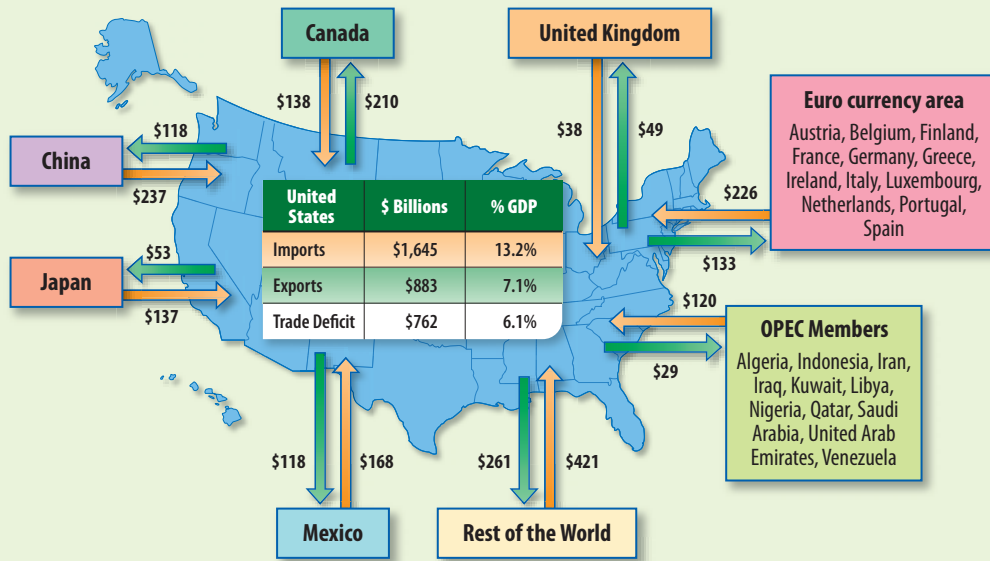
BL Rearrange each group's materials, and have them complete the activity again.

AL Have students redesign the activity using different materials.

ELL Have students create a poster depicting major items imported and exported by the United States.

The United States exports merchandise (goods) all over the world. The biggest trade imbalance is with China, followed by the OPEC members.

Economic Analysis Which single area of the world trades the most with the United States?



In billions of dollars
Source: Economic Report of the President, 2006

countries exchange are goods. However, trade in services such as banking and insurance is increasing.

Figure 16.2 shows the patterns of merchandise trade for the United States with the rest of the world. The import of goods alone amounts to \$1,645 billion, or about \$5,500 per person. The numbers in the figure would be even larger if we included the value of services.

In the end, international trade is much more than a way to obtain exotic products. The sheer volume of trade between nations with such different geographic, political, and religious characteristics is proof that trade is beneficial.

Reading Check Explaining Why is specialization a good idea in trade?

The Basis for Trade

MAIN Idea Trade works best when countries focus on those products they can produce best.

Economics and You Have you ever bought anything, such as clothing or a meal, that you could have made yourself? Read on to learn how this action relates to international trade.

It may be cheaper for a country to import a product than to manufacture it. The difference between absolute and comparative advantage makes this clear.

Absolute Advantage

A country has an **absolute advantage** when it can produce more of a product than another country. For example, assume

absolute advantage
country's ability to produce more of a given product than another country can produce

S Skill Practice

Visual Literacy Ask: What percentage of the U.S. GDP do exports represent? (7.1 percent) What is the difference in value between the United States' imports and exports with Mexico? (The United States imports \$50 billion more from Mexico than it exports to Mexico.) **OL**

D Differentiated Instruction

English Language Learners

Explain that *absolute* means "ultimate or unquestionable," while *comparative* means "related to a comparison between things." Model the use of these terms in sentences for students, and then ask students to explain the meanings in their own words. **ELL**

Economic Analysis

Answer: Euro currency area

Reading Check Answer: because it allows people to produce the things they do best and exchange those products for the things that other people do best

Leveled Activities

BL Reinforcing Economic Skills, p. 26

Reinforcing Economic Skills Activity 26

MAKING NOTES

As you read, take notes on the main ideas and details. Write down the main ideas and details in your notebook. Use the space provided to write your notes.

Reading Strategy

Read the text and answer the questions. Write your answers in the space provided.

1. What is the main idea of the text?

2. What are the details that support the main idea?

3. How does the author use evidence to support his or her claims?

4. What is the author's purpose in writing this text?

5. How does the author use language to persuade you?

6. What is the author's tone in this text?

7. How does the author use structure to organize the text?

8. What is the author's main claim?

9. How does the author use evidence to support his or her claims?

10. What is the author's purpose in writing this text?

OL Economic Concepts Transparencies, Strategies, and Activities, p. 39

ECONOMIC CONCEPTS Student Activity 20

ABSOLUTE AND COMPARATIVE ADVANTAGE AND BARRIERS TO TRADE

ABSOLUTE ADVANTAGE

A country has an absolute advantage in the production of a good if it can produce more of that good than any other country.

COMPARATIVE ADVANTAGE

A country has a comparative advantage in the production of a good if it can produce that good at a lower opportunity cost than any other country.

REASONING TO THE TRANSPARENCY

Directions: Use the transparency to answer the following questions.

1. In the cartoon, how does the law of comparative advantage affect the world?

2. According to the cartoon, what is the purpose of the law?

3. Explain what has happened in the cartoon.

GOING BEYOND THE TRANSPARENCY

Directions: Use the transparency to answer the following questions.

1. How does the law of comparative advantage affect the world?

2. What are some potential costs of this law?

AL Enrichment Activities, p. 16

ENRICHMENT Chapter 16

WORLD TRADE: U.S. EXPORTS AND IMPORTS

Using the data in the table, answer the questions. Write your answers in the space provided.

U.S. Exports and Imports by Goods, 1970 to 2000

Category of Goods	Exports	Imports	Balance
Manufactured Goods	1970	21.1	11.1
1980	100.7	100.0	0.7
1990	214.2	209.4	4.8
2000	401.1	1,000.4	-599.3
Agricultural Products	1970	7.0	1.0
1980	11.0	1.0	10.0
1990	20.0	2.0	18.0
2000	40.0	2.0	38.0

1. Describe the general trend in the export of manufactured goods between 1970 and 2000.

2. How does the trend in exports of manufactured goods compare to imports of manufactured goods in the same period?

3. Describe the trend in the export of agricultural goods between 1970 and 2000.

4. Which decade saw the greatest total increase in imported manufactured goods?

5. Which decade saw the greatest total increase in exported agricultural products?

R Reading Strategy

Reading Graphs Ask: How many pounds of cashew nuts could Alpha produce if it produced 30 million pounds of coffee? (2 million pounds) How many pounds of coffee could Beta produce if it produced 6 pounds of cashew nuts? (zero; it wouldn't produce any coffee) **BL**

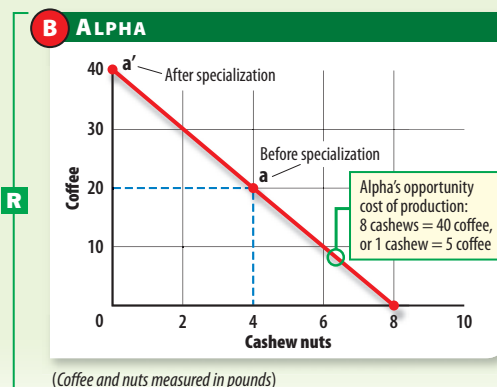
W Writing Support

Expository Writing Have students review the information about production possibilities frontiers. Then ask them to write a paragraph that identifies the information contained in the graphics and explains how to interpret them. Remind students to include brief descriptions of how these visuals can be used to pinpoint opportunity cost. **OL**

Economic Analysis

Answer: Alpha

A	Total Output Before Specializing					Total Output After Specializing				
	Alpha		Beta			Alpha		Beta		
	Coffee	20	+	5	= 25	Coffee	40	+	0	= 40
	Cashews	4	+	1	= 5	Cashews	0	+	6	= 6



production possibilities frontier diagram showing the maximum combinations of goods and/or services an economy can produce when all resources are fully employed (also see page 21)

comparative advantage country's ability to produce a given product relatively more efficiently than another country by doing it at a lower opportunity cost

opportunity cost cost of the next-best alternative use of money, time, or resources when making a choice (also see page 20)

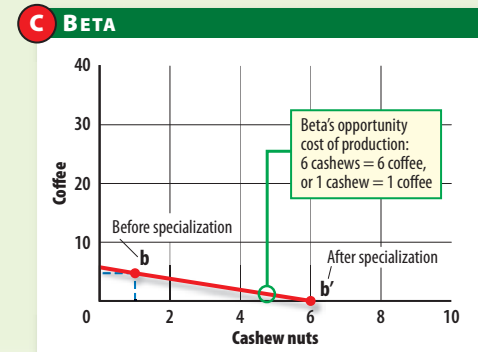
the hypothetical case of two countries—Alpha and Beta—which are the same size in terms of area, population, and capital stock. Only their climate and soil fertilities differ. In each country, only two crops can be grown—coffee and cashew nuts.

In Figure 16.3 you see an illustration of the **production possibilities frontiers** for Alpha and Beta. Note that if both countries devote all of their efforts to producing coffee, Alpha could produce 40 million pounds and Beta six million—giving Alpha an absolute advantage in the coffee production. If both countries concentrate on producing cashew nuts, Alpha could produce eight million pounds and Beta six million. Alpha, then, also has an absolute advantage in the production of cashew nuts because it can produce more than Beta.

For years, people thought that absolute advantage was the basis for trade because

▶ If Alpha and Beta each specializes in the product it can produce relatively more efficiently, total output for both countries goes up. After specialization, each country would trade its surplus production with its neighbor.

Economic Analysis Does Alpha or Beta have a comparative advantage in the production of coffee?



it enabled a country to produce enough of a good to consume domestically while leaving some for export. However, the concept of absolute advantage did not explain how two countries could benefit from an exchange in which a country with a large output like Alpha traded with a country with a smaller output like Beta.

Comparative Advantage

Even when one country enjoys an absolute advantage in the production of all goods, as in the case of Alpha above, trade between it and another country is still beneficial. This happens whenever a country has a **comparative advantage**—the ability to produce a product relatively more efficiently, or at a lower opportunity cost.

To illustrate, because Alpha can produce either 40 pounds of coffee or 8 pounds of cashew nuts, the **opportunity cost** of

Hands-On Chapter Project

Step 1

Analyzing World Trade

In this project, student groups will profile one country's international trade, exchange rates, balance of trade, and trade restrictions.

Step 1: Studying the Importance of Trade to a Nation. Student groups will study the international trade of a specific nation.

Directions: Organize the class into five different groups. Assign each of the groups one of the following continents: North America, South America, Europe, Africa, and Asia. Student groups should then select a nation located on their assigned continent to profile. The North America group should choose a nation other than the United States. Have students research the major imports, exports, absolute advantages, and

comparative advantages of their nation. Ask students to present their findings on a large poster, featuring images, statistical graphs, and text.

Display each group's completed poster in the classroom. Have members discuss their posters with the class.

Describing Ask students to write a short paper describing the importance of trade to the nation that they researched. **OL**

(Chapter Project continued in Section 2.)

producing 1 pound of cashew nuts is 5 pounds of coffee (40 pounds of coffee divided by 8). At the same time, Beta's opportunity cost of producing 1 pound of cashew nuts is 1 pound of coffee (6 pounds of coffee divided by 6). Beta is the lower-cost producer of cashew nuts because its opportunity cost of producing 1 pound of nuts is 1 pound of coffee—whereas Alpha would have to give up 5 pounds of coffee to produce the same amount of cashews.

If Beta has a comparative advantage in producing cashews, then Alpha must have a comparative advantage in coffee production. Indeed, if we try to find each country's opportunity cost of producing coffee, we would see that Alpha's opportunity cost of producing 1 pound of coffee is 1/5 of a pound of cashews (8 pounds of cashews divided by 40). Using the same computations, Beta's opportunity cost is 1 pound of cashews (6 pounds of cashews divided by 6). Alpha, then, has a comparative advantage in coffee production, because its opportunity cost of production is lower than Beta's.

The Gains from Trade

The concept of comparative advantage is based on the assumption that everyone will be better off specializing in the products they produce best. This applies to individuals, companies, states, and regions as well as to nations.

If we look at the final result of trade between Alpha and Beta, we can see that specialization and trade increased the total world output. Without trade, both countries together produced 25 coffee and 5 cashews. After trade, total world output grew to 40 coffee and 6 cashews.

This explains why countries such as the United States and Colombia trade. The United States has the necessary resources to produce farm equipment efficiently, while Colombia has the resources to produce coffee efficiently. Because each country has a comparative advantage in a product the other country wants, trade will be beneficial to both.

✓ Reading Check Summarizing Why is it beneficial for a country to trade with another when it has comparative advantage?

Economics ONLINE
Student Web Activity
 Visit the *Economics: Principles and Practices* Web site at glencoe.com and click on Chapter 16—Student Web Activities for an activity on international trade agreements.

Skills Handbook
 See page R43 to learn about **Comparing and Contrasting**.

SECTION 1

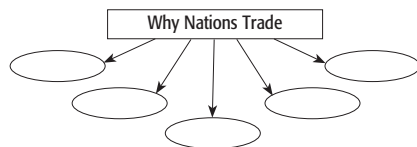
Review

Vocabulary

- 1. Explain** the significance of exports, imports, absolute advantage, and comparative advantage.

Main Ideas

- 2. Listing** Use a graphic organizer like the one below to list the reasons that nations trade with one another.



- 3. Describing** How do specialization and trade benefit both trading partners?
- 4. Explaining** Why does total world output increase as countries specialize to engage in trade?

Critical Thinking

- 5. The BIG Idea** What does the theory of comparative advantage suggest that countries should do?
- 6. Contrasting** How do comparative advantage and absolute advantage differ? Use examples to support your comparison.
- 7. Predicting** Suppose a nation has a great deal of human capital but few natural resources. In what kinds of products might the nation specialize?
- 8. Analyzing Visuals** Look at Figure 16.3 on page 444. What would happen to total output if Alpha preferred growing cashew nuts and Beta specialized in coffee?

Applying Economics

- 9. Comparative Advantage** Do you know of a product for which your state has a comparative advantage? Explain how this might affect trade with another state.

Reading Strategy

Determining Importance

Ask: What is the assumption on which the concept of comparative advantage is based? (The concept is based on the assumption that everyone will be better off specializing in the products they produce best.) **OL**

✓ Reading Check

Answer:

because it can trade a product it produces best in exchange for a product it wants that another country produces best

Assess

Use the Interactive Tutor Self-Assessment CD-ROM to review Section 1, and then assign the Section 1 Review as homework or as an in-class activity.

Close

Comparing and Contrasting

Have students draw a Venn diagram comparing and contrasting absolute and comparative advantage. **OL**

Review

SECTION 1

Answers

- All definitions can be found in the section and the Glossary.
- lack of goods at home; need for raw materials; specialization; exotic products; profit
- They allow both trading partners to produce the things they do best and exchange those products for the things that other people do best.
- because specialization allows countries to specialize in the things that they produce most efficiently
- specialize in the products that they produce best
- Absolute advantage is a country's ability to produce more of a given product than another country can produce. For instance, if country A could produce more cars than country B, country A would have an absolute advantage. Comparative advantage is a country's ability to produce a given product more efficiently than another country by doing it at a lower opportunity cost. If country B could produce cars at a lower opportunity cost than country A, it would hold the comparative advantage.
- Possible answer:** services such as financial consulting
- The production of both coffee and cashew nuts, as well as total production, would decrease.
- Students should realize that a comparative advantage might allow the state to trade for products another state produces more efficiently.



CASE STUDY

Teach

C Critical Thinking

Analyzing Ask: *Why do you think the Virgin Group was likely to have a comparative advantage in the markets it expanded into? (Branson chose markets that were either underserved or lacked competition. With the significant resources of the Virgin Group, it was likely to hold a comparative advantage in these markets.)* **OL**

Analyzing the Impact

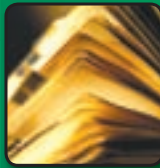
Answers:

1. It includes many individual companies united under the Virgin brand, whereas other companies are organized as a single corporation with many divisions.
2. Establishing many smaller companies that target specific markets allowed those companies to gain a comparative advantage in each market.

Additional Support

Teacher Tip

Visual Learners If you have extra time, you might suggest that students illustrate their time lines (for example, they might show a logo or product for each new company). They can create drawings or print images from the Internet showing the actual events described.



CASE STUDY

Virgin Group

Unlimited Advantage

The theory of comparative advantage has led many companies to narrow their product lines. Richard Branson, founder of Virgin Group, did just the opposite. He decided to expand into a wide range of products in an even wider geographic area. Rather than building one large corporation with many divisions, though, Branson decided to create many individual companies united under the Virgin brand. The result: companies located on most continents, selling everything from train rides and low-cost flights to music, mobile phones, and luxury vacations.



Finding Niche Markets

Virgin traces its origins back to 1968, when Branson published the first issue of Student Magazine for his university. Shortly after, he expanded into mail-order record sales and record shops. He also launched his own record label, signing such artists as Phil Collins and Boy George.

For over a decade, Branson limited his business ventures to

those related to music. During the 1980s, Branson decided to begin his expansion into other products and worldwide markets. His business plan was to find markets that are either underserved or lack competition. First steps included Virgin Atlantic Air Cargo and a luxury hotel in Spain.

Success Story

Today, Virgin Group has about 200 companies on most continents. Some provide their everyday customers with affordable vacations. Others cater to a more exclusive crowd, such as a luxury game resort in Africa and a motorcycle limousine service that can skirt London traffic jams. His latest venture will take vacationers into space. Branson's formula for success is apparently working. In 2005 the Virgin Group reported revenues of about \$8 billion.

Analyzing the Impact

1. **Recalling** How does the organization of Virgin Group differ from that of most other corporations?
2. **Drawing Conclusions** How did Branson's business plan allow him to use comparative advantage?

Virgin's Success

1968	Company begins
1970	Start of mail order record sales
1971	Opens first record shop
1973	Virgin record label launched
1984	Virgin Atlantic Airways opens
1987	Virgin Records America founded
1991	Virgin Publishing Company founded
1993	Virgin Radio begins
1999	Virgin Mobile launched
2000	Virgin Cars Produced
2002	Virgin Credit Card established

Source: www.virgin.com

Activity: Collaborative Learning

Make a Time Line Direct students to review the information presented in the chart on page 446. Then, have students work with partners to present this information on a time line. Instruct student pairs to conduct research to learn more about the Virgin Group and to then place additional entries on their time lines. Tell students to

organize their time lines logically and to include any necessary benchmark labels that will help readers better read and understand the time lines. Remind students to also include detailed labels for each time line entry. Invite volunteers to present their time lines to the class. **OL**

GUIDE TO READING

Section Preview

In this section, you will learn that nations use tariffs and quotas to protect special interests, while the free trade movement tries to eliminate trade barriers.

Content Vocabulary

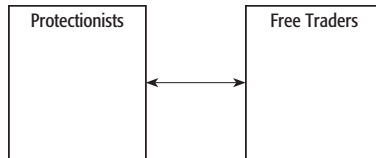
- tariff (p. 448)
- quota (p. 448)
- protective tariff (p. 448)
- revenue tariff (p. 448)
- protectionists (p. 450)
- free traders (p. 450)
- infant industries argument (p. 450)
- balance of payments (p. 452)
- most favored nation clause (p. 453)
- World Trade Organization (WTO) (p. 453)
- North American Free Trade Agreement (NAFTA) (p. 454)

Academic Vocabulary

- imposed (p. 448)
- justify (p. 450)

Reading Strategy

Describing As you read the section, complete a graphic organizer similar to the one below by describing the arguments of protectionists and free traders.



ISSUES IN THE NEWS

—www.usinfo.state.gov

China Economic Ties Under Scrutiny

U.S. Commerce Secretary Carlos Gutierrez warns that the United States might be forced to reassess its economic relationship with China if Beijing fails to address economic frictions between the two countries quickly and effectively. . . . He said that China maintains a range of non-tariff barriers that, in combination with other policies, prevent the United States from achieving balanced trade with that country. . . .

He said that “with a stroke of a pen” China could open critical closed sectors to competition from abroad. “Progress would greatly strengthen those of us who oppose protectionist policies,” Gutierrez said. But if the Chinese government refuses or fails to act quickly, the U.S. Congress might “go down a path that none of us want,” that is “build protectionist barriers around the U.S. market,” he said. ■



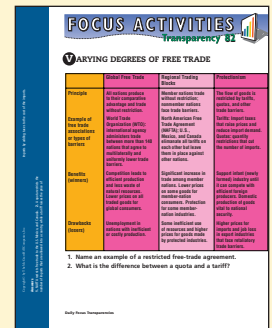
While free markets and international trade can bring many benefits, some people still object, because trade can displace selected industries and groups of workers. When these people object to trade, they look for ways to prevent it, or to at least slow the rate of growth.

Because of the wealth that a market economy can generate, China has decided to join the community of nations committed to markets and trade. China is still new at this, however, and as you read in the news story, it is trying to protect some sectors of the economy while opening up to trade.

Focus

Bellringer

Daily Focus Transparency 82



GUIDE TO READING

Answers to Graphic:

Protectionists: want to protect domestic producers against foreign competition with tariffs, quotas, and other trade barriers

Free Traders: favor fewer or even no trade restrictions

Resource Manager

R Reading Strategies

Teacher Edition

- Summarizing, p. 448
- Outlining, p. 451
- Identifying, p. 454

Additional Resources

- Guid. Read. Act., p. 47
- Read. Ess. & Note-Taking Guide, p. 139

C Critical Thinking

Teacher Edition

- Interpreting, p. 449
- Analyzing Visuals, p. 450
- Drawing Con., p. 453

Additional Resources

- Authentic Assess., p. 8
- Bus. Focus on the Global Economy, pp. 2, 10, 17

D Differentiated Instruction

Teacher Edition

- Verbal/Linguistic, p. 449
- Visual/Spatial, p. 452
- Adv. Learners, p. 453

Additional Resources

- Pri./Sec. Source Readings, p. 43
- Quizzes and Tests, p. 202

W Writing Support

Teacher Edition

- Expository Writing, p. 448
- Persuasive Writing, p. 452

Additional Resources

- High School Writing Process Trans.
- Crit. Think. Act., p. 22

S Skill Practice

Teacher Edition

- Using Geo. Skills, p. 450
- Visual Literacy, pp. 451, 455

Additional Resources

- Econ. Content Vocab. Act., p. 16
- Reading and Study Skills Fold., pp. 63, 64

Teach

R Reading Strategy

Summarizing Ask: **What are the goals of a government when levying a protective tariff and a revenue tariff?** (A government levies a protective tariff with the goal of raising the costs of imports so that domestic industries are protected from being undersold. A revenue tariff generates government revenue without prohibiting imports.) **OL**

W Writing Support

Expository Writing Have students research a time in which the U.S. government used tariffs prior to 1913. Tell students to write a short essay evaluating the government's use of the tariffs they researched. Instruct them to categorize the tariffs as either protective or revenue tariffs, and discuss whether the tariffs were successful in achieving the government's goals. **AL**

Caption Answer: protective tariff

Additional Support

tariff tax placed on an imported product

quota limit on the amount of a good that is allowed into a country

R **protective tariff** tax on an imported product designed to protect less-efficient domestic producers

revenue tariff tax placed on imported goods to raise revenue

Restricting International Trade

MAIN Idea Tariffs and quotas are the main ways to restrict international trade.

Economics and You Have you noticed where your clothes, electronics, or home appliances are made? Read on to find out about ways to restrict imports of such goods.

Historically, trade has been restricted in two major ways. One is through a **tariff**—a tax placed on imports to increase their price in the domestic market. The other is with a **quota**—a limit placed on the quantities of a product that can be imported.

Tariffs

Governments generally levy two kinds of tariffs—protective tariffs and revenue tariffs. A **protective tariff** is a tariff that is high enough to protect less-efficient domestic industries. Suppose, for example, that it costs \$1 to produce a mechanical pencil in the United States, while the same product can be imported for 35 cents from another country. If a tariff of 95 cents is placed on each imported pencil, the cost for these imports climbs to \$1.30 per pencil—more than the cost of the American-made one.

Tariffs In 2002 a temporary tariff on steel imports protected the jobs of steelworkers such as this one. **What is the name of this kind of tariff?**



448 UNIT 5 The Global Economy

The result of the tariff is that a domestic industry is protected from being undersold by a foreign one.

The **revenue tariff** is a tariff that is high enough to generate revenue for the government without actually prohibiting imports. If the tariff on imported mechanical pencils were 40 cents, the price of the imports would be 75 cents, or 25 cents less than the American-made ones. As long as the two products are identical, consumers would prefer the imported one because it is less expensive, so the tariff would raise revenue rather than protect domestic producers from foreign competition.

Traditionally, tariffs were used more for revenues than for protection. Before the Civil War, tariffs were the chief source of revenue for the federal government. From the Civil War to 1913, tariffs provided about one-half of the government's total revenue. After the federal income tax became law in 1913, the government had a new and more lucrative source of revenue. Since then tariffs—also called customs duties—have accounted for only a small portion of total government revenue, as shown in Figure 9.3 on page 239.

In practice, a tariff achieves a little bit of both goals—it gives some protection and it raises some revenue. In 2002, for example, the Bush administration **imposed** a 30 percent temporary tariff on foreign steel imports to protect the domestic steel industry. The tariff raised some revenue and preserved some jobs during an election year, but it also raised the price of domestic steel by 20 to 30 percent—and hence the cost of goods to U.S. consumers.

Quotas

Foreign goods sometimes cost so little that even a high tariff on them might not protect the domestic market. In

Activity: Collaborative Learning

Predicting One way to motivate students to read is to have them make predictions about the content beforehand and then evaluate their predictions after they read. Remind students that to make predictions, they should use what they already know combined with information from the text. Ask students to predict what

might happen if harsh trade restrictions were erected between all nations of the world. Then have students read the section, helping them as necessary. After students have finished reading, have them work in small groups to review the accuracy of their predictions. Direct students to discuss the predictions in their

groups. Encourage group members to identify the pieces of information that helped them make accurate predictions, as well as the missing information that might have made their incorrect predictions more accurate. **BL**

such cases, the government can use a quota to keep foreign goods out of the country. Quotas can even be set as low as zero to keep a product from ever entering the country. More typically, quotas are used to reduce the total supply of a product to keep prices high for domestic producers.

In 1981, for example, domestic automobile producers faced intense competition from lower-priced Japanese imports. Rather than lower their own prices, domestic manufacturers wanted President Ronald Reagan to establish import quotas on Japanese cars. The Reagan administration agreed. As a result, Americans had fewer cars from which to choose, and the prices of all cars were higher than they otherwise would have been.

More recently, the threat of a quota has been used as a way to persuade other nations to change their trade policies. For example, the United States became concerned when the low prices China charged for its exports of textiles created problems for the domestic textile industry. In order to make China raise prices, in 2005 the government threatened China with quotas on these textiles. While it may seem odd to have the U.S. government pursue policies that would raise the cost of products to American citizens, the real purpose of a quota is to protect domestic industries and the jobs in those industries.

Other Barriers

Tariffs and quotas are not the only barriers to trade. Many imported foods are subject to health inspections that are far more rigorous than those given to domestic foods. For years this tactic was used to keep beef from Argentina out of the United States. Another method is to require a license to import. If the government is slow to grant the license, or if the license fees are too high, international trade is restricted. Other nations also use health issues to restrict trade. Several European countries, for example, refuse to import genetically altered crops grown in the United States.

Nationalism and culture often play a role in these debates. Europeans frequently claim that they prefer regional and traditional foods to genetically altered ones. While these may or may not be legitimate arguments, they do restrict trade.

✓Reading Check **Comparing** How do tariffs and quotas differ?

CAREERS

Customs Inspector **D**

The Work

- * Inspect cargo, baggage, and articles worn or carried by people, vessels, vehicles, trains, and aircraft entering or leaving the United States
- * Examine, count, measure, weigh, gauge, and sample commercial and noncommercial cargoes entering and leaving the United States
- * Seize prohibited or smuggled articles and intercept contraband
- * Apprehend, search, detain, and arrest violators of U.S. laws

Qualifications

- * Must be a U.S. citizen between 21 and 36 years of age when hired
- * Possess a valid driver's license and pass a civil service exam
- * Must pass a background investigation, meet certain health requirements, and undergo a drug screening test
- * Bachelor's degree and one year of related work experience

Earnings

- * Starting annual salary: \$35,100

Job Growth Outlook

- * Average

Source: *Occupational Outlook Handbook*, 2006–2007 Edition



C Critical Thinking

Interpreting Ask: Why might the U.S. government pursue a trade policy that would raise the costs of products for American consumers? (to protect domestic industries and the jobs of workers in those industries) **OL**

D Differentiated Instruction

Verbal/Linguistic Direct students to use the content in the feature to compose a short job listing for a customs inspector. Students should summarize the position's responsibilities, qualifications, and salary. Encourage students to review job listings in the classified section of a newspaper or online help-wanted ads for guidance when writing their listings. **OL**

✓Reading Check Answer: A tariff is a tax placed on an imported product. A quota is a limit on the amount of a good that is allowed into the country.

Additional Support

Activity: Interdisciplinary Connection

Speech **Tell students:** You are the president of a nation with a relatively healthy economy. However, one of your major industries—computer parts—is in decline, largely because of foreign competition. Members of your political party who represent districts where computer parts are the main industry want a high tariff on imported computer parts. In addition, workers in the computer parts

industry have launched a huge publicity campaign in support of a tariff increase. At the same time, many people are calling for no tariff because they want to be able to buy inexpensive computer parts.

Have students explain what they, as leaders, intend to do and why. Have them write their decision in the form of a speech to be made to the nation. Invite students to give their speeches to the class. **AL**

Teacher Tip

Public Speaking Before students make their speeches, review several public speaking strategies. For example, remind students to make eye contact with every listener, speak slowly and clearly, and practice their speeches beforehand.

S Skill Practice

Using Geography Skills Have students use library and Internet resources to locate resource maps of the United States. Direct them to study the maps and evaluate how the nation's resources might allow it to prepare for war. Then have students use the maps to explain why the United States might seek to institute trade protection for the purpose of national defense. **AL**

C Critical Thinking

Analyzing Visuals **Ask:** *How might trade protection help a company such as Harley-Davidson become a worldwide competitor?* (Possible answer: Trade protection might allow such a company to improve its production process. This might help it make its products more inexpensively or improve its products' quality.) **OL**

Caption Answer: because they think that new industries need to gain strength and experience before they can compete against established industries

Additional Support

protectionist person who wants to protect domestic producers against foreign competition with tariffs, quotas, and other trade barriers

free trader person who favors fewer or even no trade restrictions

infant industries argument argument that new and emerging industries should be protected from foreign competition until they are strong enough to compete

Arguments for Protection

MAIN Idea Protectionists disagree with free traders over the best way to protect a country's independence, industries, and workers.

Economics and You What might you be willing to do to ensure the well-being of your family? Read on to learn why protectionists want to limit international trade.

Freer international trade has been a subject of debate for many years. **Protectionists** are people who favor trade barriers to protect domestic industries. Other people, known as **free traders**, prefer fewer or even no trade restrictions. The debate between the two groups usually centers on the six arguments for protection discussed below.

Aiding National Defense

S The first argument for trade barriers centers on national defense. Protectionists argue that without trade barriers, a country could become so specialized that it would end up becoming too dependent on other countries.

During wartime, protectionists argue, a country might not be able to get critical supplies such as oil and weapons. As a

result, some smaller countries such as Israel and South Africa have developed large armaments industries to prepare for such crises. They want to be sure they will have a domestic supply should hostilities break out or other countries impose economic sanctions such as boycotts.

Free traders admit that national security is a compelling argument for trade barriers. They believe, however, that the advantages of having a reliable source of domestic supply must be weighed against the disadvantages that the supply will be smaller and possibly less efficient than it would be with free trade.

The political problem of deciding which industries are critical to national defense and which are not must also be considered. At one time, the steel, automobile, ceramic, and electronics industries all have argued that they are critical to national defense and so should receive some protection.

Promoting Infant Industries

The **infant industries argument**—that new or emerging industries should be protected from foreign competition—is also used to **justify** trade barriers. Protectionists claim that some industries need to gain

Protecting Industries While Harley-Davidson was not a new industry at the time, trade protection in the 1980s helped it to retool and become a worldwide competitor. **Why do protectionists believe that new industries need protection?**



Activity: Hands-On Economics

Hold a Classroom Debate Organize students into three groups. Assign two groups the pro or con position on the following proposition: *U.S. industries should be protected from foreign competition.* Instruct the two groups to review the relevant content from the text regarding their assigned positions. Encourage group members to conduct additional research to strengthen their arguments in preparation

for the debate. Have the third group act as moderators for the debate. Tell these students to study the important issues related to trade protection and prepare a series of debate questions that address these topics. When students have completed their preparations, carry out the debate by having the group of moderators take turns asking questions of the other two groups. Assign specific

amounts of time for groups to respond to these questions, as well as to offer rebuttals to the opposing teams' responses.

After the debate, discuss as a class students' opinions about the strengths and weaknesses of the experience. Have the moderators declare a winner and explain how they arrived at their decision. **OL**

strength and experience before they can compete against established industries in other countries. Trade barriers, they argue, would give them the time they need to develop.

Many people are willing to accept the infant industries argument, but only if protection will eventually be removed so that the industry is forced to compete on its own. The problem is that industries that become accustomed to having protection are often unwilling to give it up, making for difficult political decisions later on.

To illustrate, some Latin American countries have used tariffs to protect their own infant automobile industries, with tariffs as high as several hundred percent. In some cases, the tariff raised the price of used American-made cars to more than double the cost of new ones in the United States. In spite of this protection, no country in Latin America has been able to produce a globally competitive automobile on its own. To make matters worse, governments have come to rely on the revenue supplied by tariffs, so prices for automobiles remain high for their citizens.



Outsourcing Protectionists fear that U.S. jobs might move to other countries and Americans will become unemployed. *Why do free traders disagree with this reasoning?*

Protecting Domestic Jobs

A third argument—and the one used most often—is that tariffs and quotas protect domestic jobs from cheap foreign labor. Workers in the shoe industry, for example, have protested the import of lower-cost Italian, Spanish, and Brazilian shoes. Garment workers have opposed the import of lower-cost Korean, Chinese, and Indian clothing. Some steelworkers have even blocked foreign-made cars of coworkers from company parking lots to show their displeasure with the foreign-made steel components in the cars.

In the short run, protectionist measures provide temporary protection for domestic jobs. This is especially attractive to people who want to work in the communities where they grew up. In the long run, however, industries that find it difficult to compete today will find it even more difficult

R to compete in the future unless they change the way they operate. As a result, most free traders believe that it is best not to interfere, thereby keeping the pressure on threatened industries to modernize and improve.

When inefficient industries are protected, the economy produces less and the standard of living goes down. Because of artificially high prices, people buy less of everything, including those goods produced by the protected industries. If the prices of protected products get too high, people look for substitute products, and the jobs that were supposed to be protected will still be lost. Free traders argue that the profit-and-loss system is one of the major features of the American economy and should be allowed to work. Profits reward the efficient and hard working, while losses eliminate the inefficient and weak.

R Reading Strategy

Outlining Direct students to reread the information in the subsection. Ask them to produce an outline that organizes the main ideas and important details from this text. Remind students that their outlines should be written in their own words and should not include complete sentences. Have students compare their completed outlines with partners, making revisions if necessary. **BL**

S Skill Practice

Visual Literacy Ask: *What point does the cartoonist make about the jobs of workers at the company pictured?* (The cartoonist points out that because the company has outsourced all of its work, there are no longer jobs available to domestic workers.) **OL**

Caption Answer: Free traders disagree because they believe it is best to keep pressure on threatened industries to modernize and improve.

Hands-On Chapter Project

Step 2

Analyzing World Trade

Step 2: Examining Trade Restrictions.

Student groups will create scenarios describing the effects of a trade restriction against a specific product.

Directions: Have students reassemble into their groups. Tell students to “create” a product that could be manufactured in one or more of the countries on their assigned continent. Groups should provide a written or visual description of their

product. Next, have groups devise a scenario in which people in the United States want to restrict the importation of the product. Students may use any plausible reason for this agenda (for example, domestic producers of the item are losing business to foreign competition or human rights groups oppose the foreign government’s domestic policies). Ask groups to include in their scenarios a description of the implementation of a trade restriction against the product, and the subsequent

impact—both home and abroad—of this trade barrier.

Have each group present its scenario to the class in a multimedia format or a skit. After each group has presented, discuss the immediate and long-term effects of trade barriers.

Personal Writing Have students write a short paper expressing their opinions about free trade. **OL**

(Chapter Project continued in Section 3.)

D Differentiated Instruction

Visual/Spatial Direct students to draw a cartoon of their own that focuses on an important issue surrounding trade protection. Remind students to include labels and captions to help convey their message. **OL**

W Writing Support

Persuasive Writing Ask students to write a brief persuasive essay in which they argue either for or against protection on the basis of national pride. Direct them to support their arguments using evidence from the text or other reference materials. **OL**

Caption Answer: Domestic companies can sell more of their products to consumers.

✓Reading Check **Answer:** Answers will vary, but students should provide valid reasons for their position.

Differentiated Instruction

Limiting Imports
With fewer imports, domestic companies can sell more of their products. *What happens when imports are limited?*

D



Tom Pisk/Caroonstock

"I move we go on record for fewer imports here and more imports there!"

balance of payments
difference between money paid to, and received from, other nations in trade

Keeping the Money at Home

Another argument for trade barriers claims that limiting imports will keep American money in the United States instead of allowing it to go abroad. Free traders, however, point out that the American dollars that go abroad generally come back again. The Japanese, for example, use the dollars they receive for their automobiles to buy American cotton, soybeans, and airplanes. These purchases benefit American workers in those industries.

The same is true of the dollars used to buy oil from the Middle East. The money comes back to the United States when oil-rich foreigners buy American-made oil technology. Keeping the money at home also hurts those American industries that depend on exports for their jobs.

Helping the Balance of Payments

Another argument in the free trade debate involves the **balance of payments**—the difference between the money a country pays out to, and receives from, other

nations when it engages in international trade. Protectionists argue that restrictions on imports reduce trade deficits and thus help the balance of payments.

Protectionists overlook the dollars that return to the United States to stimulate employment in other industries. As a result, most economists do not believe that interfering with free trade can be justified on the grounds of helping the balance of payments.

National Pride

A final argument for protection is national pride. France, for example, is proud of its wines and cheeses and protects those industries for nationalistic reasons. In the 1980s, the United States gave temporary protection to Harley-Davidson, an American icon. Whether this is a good idea depends on how long the protection lasts. If it is permanent, then the government is simply protecting inefficient producers.

✓Reading Check **Synthesizing** Do you agree with the protectionists' arguments or those of the free traders? Why?

Free Trade and Jobs

- Objective:** Understand how free trade has affected U.S. jobs.
- Focus/Teach:** Ask students how free trade has impacted the U.S. labor force. Then have students complete the activity.
- Assess:** Review the answers as a class, discussing any that give students difficulty.
- Close:** Ask students to write a paragraph explaining their opinions on NAFTA.

Differentiated Instruction Strategies

BL Ask: In which two states did workers suffer the greatest loss in pay? (New York, Kansas)

AL Have students research and then write a short report on the TAA program.

ELL Ask students to use the data in the table to create a bar graph for each region.

FREE ENTERPRISE ACTIVITY 22

FREE TRADE AND JOBS

The United States Trade Representative (USTR) Program monitors international trade policy. The USTR's Office of Trade Policy and Negotiation (OTPN) is responsible for the U.S. trade policy. The OTPN's mission is to ensure that U.S. trade policy is consistent with the U.S. Constitution and the U.S. Trade Policy Agenda. The OTPN's mission is to ensure that U.S. trade policy is consistent with the U.S. Constitution and the U.S. Trade Policy Agenda.

Table 1: U.S. Trade Policy Agenda (2000-2001)

Region	U.S. Trade Policy Agenda (2000-2001)	U.S. Trade Policy Agenda (2000-2001)	U.S. Trade Policy Agenda (2000-2001)	U.S. Trade Policy Agenda (2000-2001)
North America	U.S. Trade Policy Agenda (2000-2001)	U.S. Trade Policy Agenda (2000-2001)	U.S. Trade Policy Agenda (2000-2001)	U.S. Trade Policy Agenda (2000-2001)
Europe	U.S. Trade Policy Agenda (2000-2001)	U.S. Trade Policy Agenda (2000-2001)	U.S. Trade Policy Agenda (2000-2001)	U.S. Trade Policy Agenda (2000-2001)
Asia	U.S. Trade Policy Agenda (2000-2001)	U.S. Trade Policy Agenda (2000-2001)	U.S. Trade Policy Agenda (2000-2001)	U.S. Trade Policy Agenda (2000-2001)
Latin America	U.S. Trade Policy Agenda (2000-2001)	U.S. Trade Policy Agenda (2000-2001)	U.S. Trade Policy Agenda (2000-2001)	U.S. Trade Policy Agenda (2000-2001)
Middle East	U.S. Trade Policy Agenda (2000-2001)	U.S. Trade Policy Agenda (2000-2001)	U.S. Trade Policy Agenda (2000-2001)	U.S. Trade Policy Agenda (2000-2001)
Africa	U.S. Trade Policy Agenda (2000-2001)	U.S. Trade Policy Agenda (2000-2001)	U.S. Trade Policy Agenda (2000-2001)	U.S. Trade Policy Agenda (2000-2001)
Oceania	U.S. Trade Policy Agenda (2000-2001)	U.S. Trade Policy Agenda (2000-2001)	U.S. Trade Policy Agenda (2000-2001)	U.S. Trade Policy Agenda (2000-2001)
Other	U.S. Trade Policy Agenda (2000-2001)	U.S. Trade Policy Agenda (2000-2001)	U.S. Trade Policy Agenda (2000-2001)	U.S. Trade Policy Agenda (2000-2001)

The Free Trade Movement

MAIN Idea Because tariffs hurt more than they helped during the Great Depression, the United States has found ways to reduce trade restrictions.

Economics and You You learned about the Great Depression in your history courses. Read on to find out how tariffs during that time have affected international trade today.

The use of trade barriers to protect domestic industries and jobs works only if other countries do not retaliate with their own trade barriers. If they do, all countries suffer, because they have neither the benefits of efficient production nor access to less costly products and raw materials from other nations.

Tariffs During the Great Depression

In 1930 the United States passed the Smoot-Hawley Tariff Act, one of the most restrictive tariffs in history. It set import duties so high that the prices of many imported goods rose nearly 70 percent. When other countries did the same, international trade nearly came to a halt.

Before long, most countries realized that high tariffs hurt more than they helped. As a result, in 1934 the United States passed the Reciprocal Trade Agreements Act, which allowed it to reduce tariffs up to 50 percent if other countries agreed to do the same. The act also contained a **most favored nation clause**—a provision allowing a country to receive the same tariff reduction that the United States gives to any third country.

Suppose, for example, that the United States and China have a trade agreement with a most favored nation clause. If the United States then negotiates a tariff reduction with a third country

such as Canada, the reduction would also apply to China. This clause is very important to China, because its goods will then sell at an even lower price in the American market.

The World Trade Organization

In 1947, 23 countries signed the General Agreement on Tariffs and Trade (GATT). The GATT extended tariff concessions and worked to eliminate import quotas. Later, the Trade Expansion Act of 1962 gave the president of the United States the power to negotiate further tariff reductions. As a result of this legislation, more than 100 countries agreed to reduce the average level of tariffs by the early 1990s.

More recently, GATT was replaced by the **World Trade Organization (WTO)**, an international agency that administers trade agreements signed under GATT. The WTO also settles trade disputes between nations, organizes trade negotiations, and provides technical assistance and training for developing countries.

Because so many countries have been willing to reduce tariffs and quotas under GATT and the WTO, international trade is flourishing. Tariffs that in the past nearly doubled the price of many goods now increase prices by only a small percentage. Other tariffs have been dropped altogether.

most favored nation clause trade law allowing another country to enjoy the same tariff reductions the United States negotiates with any third country

World Trade Organization (WTO) international agency that administers trade agreements, settles trade disputes between governments, organizes trade negotiations, and provides technical assistance and training for developing countries

World Trade Organization Regular meetings of the WTO assist in smoothing out or eliminating trade disagreements. **Why do countries enter trade agreements?**



CHAPTER 16, SECTION 2

C Critical Thinking

Drawing Conclusions

Ask: What do you think might prompt a country like the United States to offer a most favored nation clause to another nation? (Possible answer: The United States would likely offer the clause because the nation is a major trading partner and the United States wants to preserve a beneficial trading relationship with the nation.) OL

D Differentiated Instruction

Advanced Learners Ask students to research the World Trade Organization, including its members, structure, and key responsibilities. Ask students to use their findings to produce a report on the WTO and its role in international trade. Encourage students to include charts, graphs, or other visuals that they feel may enhance their essays. AL

Caption Answer: to maintain conditions for international trading that benefit all of the nations involved

Leveled Activities

BL Reading Essentials and Note-Taking Guide, p. 139

OL Primary and Secondary Source Readings, p. 43

AL BusinessWeek Focus on the Global Economy, p. 10

Chapter 16, Section 2 (Pages 447-449)

Barriers to International Trade

Big Idea As you read pages 447-449 in your textbook, complete this graphic organizer by describing the arguments of protectionists and free traders.

Protectionists	Free Traders
<p>Notes</p> <p>Read to Learn</p> <p>Predicting</p> <p>1. What might happen if a government did not impose a protective tariff on steel products?</p> <p>2. How would our manufacturing be affected?</p>	<p>Government exists to protect industries. One common way to protect trade is through a tariff—a tax placed on imports to increase their price in the domestic market.</p> <p>One kind of tariff is a protective tariff, or tax designed to protect domestic industries by raising the price of goods from other countries. As a result, tariffs protect domestic producers from foreign competition.</p> <p>The other type of tariff is a revenue tariff, which generates revenue for a government without protecting traders.</p> <p>Historically, the U.S. government has relied on both of these revenue through revenue tariffs. In 1913, the government ended a more profitable revenue source—the federal income tax.</p> <p>Governments also protect trade by setting quotas. This is the limit on the amount of a product that is allowed into a country. Quotas successfully protect domestic businesses and jobs even when high tariffs do not.</p> <p>Other barriers to trade include health inspections and import licenses. Nationalism and culture influence both of these.</p>

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PRIMARY & SECONDARY SOURCES Reading 22

TRADING BLOCKS

Read America's long and tangled history as a nation of protecting jobs and providing a better standard of living. Then, read America's long and tangled history as a nation of protecting jobs and providing a better standard of living. Then, read America's long and tangled history as a nation of protecting jobs and providing a better standard of living.

By the way, the night protectionists consistently are losing ground, more goods are shipped across more borders all the time.

Since 1980, Congress has passed the Trade Agreements Act, which allows the president to negotiate trade agreements with other countries. This act has led to a significant reduction in trade barriers between the United States and other nations.

The Trade Agreements Act of 1980 gave the president the authority to negotiate trade agreements with other countries. This act has led to a significant reduction in trade barriers between the United States and other nations.

The Trade Agreements Act of 1980 gave the president the authority to negotiate trade agreements with other countries. This act has led to a significant reduction in trade barriers between the United States and other nations.

BusinessWeek Focus on the Global Economy, p. 10

Walling Off Growth

With industry after industry being protected by tariffs and quotas, the growth of the U.S. economy is being held back. The growth of the U.S. economy is being held back by the growth of the U.S. economy.

The growth of the U.S. economy is being held back by the growth of the U.S. economy. The growth of the U.S. economy is being held back by the growth of the U.S. economy.

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The growth of the U.S. economy is being held back by the growth of the U.S. economy. The growth of the U.S. economy is being held back by the growth of the U.S. economy.

R Reading Strategy

Identifying Ask: What three major trading partners created NAFTA in 1993? (the United States, Canada, and Mexico) **BL**

✓Reading Check Answer: The WTO helped countries reduce tariffs and quotas, which has allowed international trade to flourish. Stores can now offer a wide variety of industrial and consumer goods from all over the world.

Assess

Use the Interactive Tutor Self-Assessment CD-ROM to review Section 2, and then assign the Section 2 Review as homework or as an in-class activity.

Close

Sequencing Information

Have students work in pairs to make a simple time line showing important developments in the free trade movement. **OL**

North American Free Trade Agreement (NAFTA)
agreement signed in 1993 to reduce tariffs and increase trade among the United States, Canada, and Mexico

Skills Handbook
See page R55 to learn about Determining Averages.

As a result, stores are able to offer a wide variety of industrial and consumer goods from all over the world.

NAFTA

The **North American Free Trade Agreement (NAFTA)** is an agreement to liberalize free trade by reducing tariffs among three major trading partners: Canada, Mexico, and the United States. It was a bipartisan agreement proposed by President George Bush and concluded by the Clinton administration in 1993.

Before NAFTA, U.S. goods entering Mexico faced tariffs averaging 10 percent. At the same time, approximately half of the goods entering the United States from Mexico were duty free, while the other half faced taxes averaging only 4 percent. NAFTA terms outlined a phase-out of tariffs among the three countries over a 15-year period.

Free trade is beneficial in general, but it is not painless. NAFTA was controversial specifically because some workers would be displaced when trade barriers were lowered. Opponents predicted that some high-paying American jobs would be lost to Mexico. Proponents predicted that trade among all three nations would increase dramatically, stimulating growth and bringing a wider variety of lower-cost goods to everyone.

Some of the costs and benefits identified during the NAFTA debate actually occurred, but not to the extent originally predicted. Trade among the three countries has grown steadily since NAFTA was created. In the end, freer trade has allowed the NAFTA partners to capitalize on their comparative advantages for everyone's benefit.

✓Reading Check Recalling How did the WTO help international trade?

SECTION

2

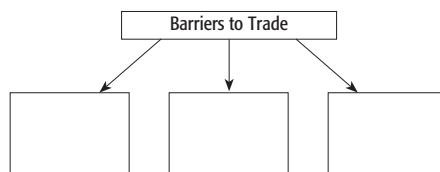
Review

Vocabulary

- 1. Explain** the significance of tariff, quota, protective tariff, revenue tariff, protectionists, free traders, infant industries argument, balance of payments, most favored nation clause, World Trade Organization (WTO), and North American Free Trade Agreement (NAFTA).

Main Ideas

- 2. Describing** Use a graphic organizer like the one below to describe three barriers to international trade.



- 3. Listing** What six arguments are commonly used to support the protectionists' views on trade?
- 4. Describing** What happened to tariffs during the Great Depression?

Critical Thinking

- 5. The BIG Idea** How do the views of protectionists and free traders differ?
- 6. Drawing Conclusions** If you, as a member of Congress, were approached by a delegation of autoworkers seeking additional tariff or quota protection, how would you respond? Defend your response.
- 7. Synthesizing** How would a high tariff on sugar affect U.S. sugar producers, manufacturers of products containing sugar, consumers, workers in the sugar industry, and workers in other related businesses?
- 8. Analyzing Visuals** Look at the cartoon on page 452. Explain the meaning of "fewer imports here and more imports there" as it relates to the balance of payments.

Applying Economics

- 9. Quotas and Tariffs** Suppose you were in charge of trade policy for the United States. Would you recommend that we increase or decrease trade barriers on athletic shoes? Explain your answer.

SECTION

2

Review

Answers

- All definitions can be found in the section and the Glossary.
- Possible answers:** tariffs, quotas, health inspections, licenses, health issues
- aiding national defense, promoting infant industries, protecting domestic jobs, keeping money at home, helping the balance of payments, national pride
- A restrictive tariff known as the Smoot-Hawley Tariff Act raised the prices of imports and caused other countries to do the same. International trade nearly stopped.

- In general, protectionists favor trade barriers to protect domestic industries; free traders prefer fewer trade barriers.
- Answers will vary, but students should offer evidence to support their position.
- U.S. sugar producers will benefit from reduced competition; manufacturers of products containing sugar will pay higher prices for sugar; workers in the sugar industry will keep their jobs, while workers in related industries could see job

layoffs; U.S. consumers will pay more for sugar and products containing sugar.

- The balance of payments is the difference between the money a country pays out to, and receives from, other nations when trading. "Fewer imports here and more imports there" suggests that by importing less and exporting more, the country can improve its balance of payments.
- Answers will vary but should demonstrate an understanding of trade barriers.

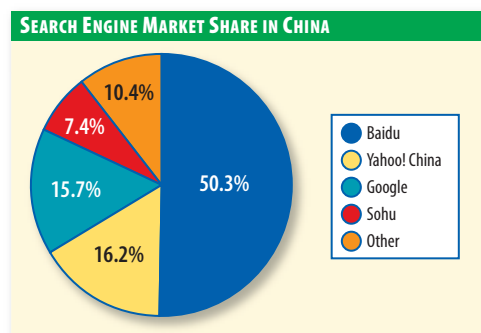
Barriers to international trade include tariffs, quotas, and . . . censorship? Before Yahoo!, Google, and other U.S. tech companies enter the Chinese search engine market, they must censor themselves. With more than 110 million Chinese using the Internet, censoring online content is evidently worth the profits generated.

The Great Firewall of China

It's no secret that Western Internet companies have to hew to the party line if they want to do business in China. Google, Yahoo!, and scores of other outfits, both domestic and foreign, have made concessions to China's censors. . . .

Getting a phone call from the government is one part of the picture. What few Westerners know is the size and scope of China's censorship machine and the process by which multinationals, however reluctantly, censor themselves. Few also know that China's censors have kept up with changing technologies, from cell phone text messaging to blogs.

How do the Chinese do it? Beijing has a vast infrastructure of technology to keep an eye on any potential online dissent. It also applies lots of human eyeballs to monitoring. The agencies that watch over the Net employ more than 30,000 people to prowl Web sites, blogs, and chat rooms on the lookout for offensive content as well as scammers. In the U.S., by contrast, the entire CIA employs an estimated 16,000 people.



Companies, both foreign and domestic, also abet the government's efforts. Virtually all Net outfits on the mainland are given a confidential list of hundreds of banned terms they have to watch for. . . .

The restrictions have led many companies to make both subtle and substantial changes to their operations. . . . IDG Venture Technology Investment . . . has invested in a Chinese company that operates online bulletin boards on real estate, entertainment, technology, autos, and more. But "we don't touch politics at all," says Quan Zhou, managing director of the group's Chinese arm. . . . Not that such policies deter investors.

—Reprinted from *BusinessWeek*

Examining the Newsclip

- Summarizing** How does China censor Internet traffic?
- Making Connections** Why is censorship a form of trade barrier?

CHAPTER 16 International Trade 455

Activity: Hand-On Economics

Complying With Censorship Ask students to use library and Internet resources to learn more about the ways in which Western Internet companies comply with Chinese censorship regulations for search engine content. Have students organize the findings from their research and produce a report summarizing what they learned. Encourage students to include any charts, graphs, or fact sheets that may enhance the content of their

reports. When students have completed their reports, lead the class in a discussion of whether companies such as those discussed in the feature should agree to censor their content in order to receive the profits generated. Tell students that they should support their arguments using evidence they found through their research. **AL**

Teach

S Skill Practice

Visual Literacy Ask: What percent of the search engine market does Yahoo! China hold? (16.2%) Which company holds the largest share of this market? (Baidu) The smallest? (Sohu) **BL**

BusinessWeek ONLINE

To find up-to-date news and analysis on the economy, business, technology, markets, entrepreneurs, investments, and finance, have students search feature articles and special reports on the BusinessWeek Web site, www.businessweek.com.

Examining the Newsclip

Answers:

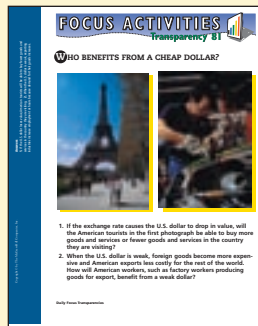
- through human monitors and a vast infrastructure of technology
- because it limits the ability of Western Internet companies to offer their products in China

Additional Support

Focus

Bellringer

Daily Focus Transparency 81



GUIDE TO READING

Possible Answers to Graphic:

Effect: The foreign exchange market is flooded with dollars.

Effect: The dollar loses some of its value.

Effect: Imports become more expensive for Americans.

Effect: Exports become less expensive for foreigners.

Resource
Manager

Foreign Exchange and Trade Deficits

GUIDE TO READING

Section Preview

In this section, you will learn that a long-lasting trade deficit affects the value of a nation's currency as well as the value and volume of its exports and imports.

Content Vocabulary

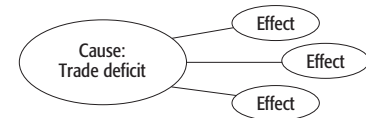
- foreign exchange (p. 457)
- foreign exchange rate (p. 457)
- fixed exchange rates (p. 457)
- flexible exchange rates (p. 458)
- floating exchange rates (p. 458)
- trade deficit (p. 460)
- trade surplus (p. 460)
- trade-weighted value of the dollar (p. 460)

Academic Vocabulary

- secure (p. 457)
- persistent (p. 460)

Reading Strategy

Describing As you read this section, complete a graphic organizer similar to the one below by describing the effects of a long-lasting trade deficit.



ISSUES IN THE NEWS

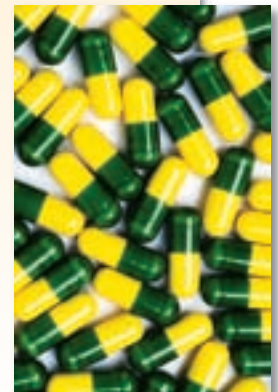
—BusinessWeek

A Ray of Hope for the Trade Gap

In recent years the U.S. trade deficit has been the No. 1 blight on an otherwise robust economy. Its persistent widening has fueled trade tensions around the world, outsourcing worries among workers, and protectionist sentiment in Washington. Is there a chance for improvement in the trade gap anytime soon?

Well, don't look for outright shrinkage, but the emerging strength in exports is the best sign yet that the rate of deterioration is slowing and that the deficit may even level off later this year.

... Overseas demand is picking up as economies from Japan to Europe shake off the blahs of recent years. ... The other big plus in the export outlook is the dollar's renewed decline, which will give U.S. goods an extra bit of competitiveness in many global markets. ■



Skills Handbook

See page R38 to learn about **Distinguishing Fact From Opinion.**

The decline in the value of the American dollar, as you read in the news story above, helped exports by making goods made in the United States cheaper for the rest of the world to buy.

It turns out that this is simply a matter of supply and demand. Whenever people in other countries sell their American dollars, the worldwide supply of dollars increases,

and the value of the dollar declines. If people in other countries decide to buy more American dollars, then the decrease in supply of dollars on world markets drives up the value of the dollar.

As a result, the value of the dollar, euro, yen, and most other international currencies tends to fluctuate daily with changes in supply and demand.

R Reading Strategies

Teacher Edition

- Reading Charts, pp. 457, 466
- Reading Graphs, p. 460

Additional Resources

- Guid. Read. Act., p. 48
- Read. Ess. & Note-Taking Guide, p. 142

C Critical Thinking

Teacher Edition

- Det. Cause/Effect, p. 459
- Synthesizing, p. 461

Additional Resources

- Econ. Concepts Trans., Strat. and Act., p. 41
- Econ. Forms and Fin. Pages Trans., Strat. and Act., p. 26

D Differentiated Instruction

Teacher Edition

- ELL, p. 457
- Verbal/Linguistic, p. 460

Additional Resources

- Authentic Assess., p. 25
- Bus. Focus on the Global Economy, p. 25

W Writing Support

Teacher Edition

- Expository Writing, pp. 458, 467
- Personal Writing, p. 462

Additional Resources

- High School Reading in the Content Area Strat. and Act.

S Skill Practice

Teacher Edition

- Using Line Graphs, p. 458
- Visual Literacy, p. 459

Additional Resources

- Hands-On Economics, p. 24
- Reinforcing Econ. Skills, p. 20

Financing International Trade

MAIN Idea International trade relies on the ability to exchange foreign currencies.

Economics and You Have you ever seen a coin or bill from another country? Read on to learn how the exchange rates for currencies are determined.

Scenarios like the following occur every day around the globe. A clothing firm in the United States wants to import business suits from a company in Great Britain. Because the British firm pays its bills in the British currency, called “pound sterling,” it also wants to receive all of its payments in pound sterling. Therefore, the American firm must sell its American dollars to buy British pounds.

Foreign Exchange

In the field of international finance, **foreign exchange**—different currencies used to facilitate international trade—are bought and sold in the foreign exchange market. This market includes banks that help **secure** foreign currencies for importers, as well as banks that accept foreign currencies from exporters.

Suppose that one pound sterling, or £1, is equal to \$1.89. If the business suits are valued at £1,000 in London, the American importer can go to a U.S. bank and buy a £1,000 check for \$1,890 plus a small service charge. The American firm then pays the British merchant in pounds, and the suits are shipped.

American exporters sometimes accept foreign currency or checks written on foreign banks in exchange for their goods. They deposit the payments in their own banks, which helps the U.S. banking system build a supply of foreign currency. This currency can then be sold to American firms that want to import goods from other countries. As a result, both the importer and the exporter end up with the currency they need.

The **foreign exchange rate** is the price of one country’s currency in terms of another country’s currency. The rate can be quoted in terms of the United States dollar equivalent, as in \$1.89 = £1, or in terms of foreign currency units per United States dollar, as in £0.5291 = \$1. The rate is reported both ways, as shown in the foreign currency listings in **Figure 16.4**.

Fixed Exchange Rates

Today, two major kinds of exchange rates exist—fixed and flexible. For most of the 1900s, the world depended on the use of **fixed exchange rates**—a system under

foreign exchange
various currencies
used to conduct
international trade

**foreign exchange
rate** price of one
country’s currency in
terms of another
country’s currency

**fixed exchange
rate** system under
which the values of
currencies are fixed in
relation to one another

Figure 16.4 Foreign Exchange Rates

Exchange Rates, May 12, 2006		
Country	U.S. \$ Equivalent	Currency per U.S. \$
Australia (dollar)	0.7728	1.2940
Brazil (real)	0.4686	2.1340
Britain (pound)	1.8900	0.5291
Canada (dollar)	0.9021	1.1085
China (yuan)	0.1249	8.0056
Denmark (krone)	0.1729	5.7841
EU (euro)	1.2888	0.7759
Hong Kong (dollar)	0.1290	7.7532
India (rupee)	0.0223	44.8900
Japan (yen)	0.0091	110.4900
Malaysia (ringgit)	0.2791	3.5825
Mexico (peso)	0.0905	11.0525
South Africa (rand)	0.1603	6.2375
South Korea (won)	0.0011	932.7662
Sri Lanka (rupee)	0.0097	102.6500
Sweden (krona)	0.1377	7.2632
Switzerland (franc)	0.8319	1.2020
Thailand (bhat)	0.0264	37.900

Source: finance.yahoo.com

► Exchange rates change constantly according to the supply and demand for different national currencies.

Economic Analysis About how many Japanese yen equal one U.S. dollar?

CHAPTER 16, SECTION 3

Teach

D Differentiated Instruction

English Language Learners

Guide English language learners in understanding the term *fixed exchange rates*. Point out that in addition to meaning “repaired or mended,” the term *fixed* also means “to set absolutely or definitely.” Invite volunteers to repeat this definition and apply it to the concept of fixed exchange rates. **ELL**

R Reading Strategy

Reading Charts Have students study the chart showing foreign exchange rates. **Ask:** Which foreign currency has a value most similar to that of the U.S. dollar? (Canadian dollar) Which type of foreign currency has the lowest value? (South Korean won) The highest value? (British pound) **OL**

Economic Analysis

Answer: about 933 Japanese yen

Additional Support

Activity: Interdisciplinary Connection

Mathematics Write the following exchange rate problems on the board, and have students solve them:

1. A television set sells for ¥52,500 in Tokyo. How much would it cost in U.S. dollars if the exchange rate was ¥110 = \$1.00? ($52,500 \div 110 = \477.27)
2. A clock in London sells for £200. How much would it cost in U.S. dollars if the exchange rate was £1 = \$1.62? ($200 \times 1.62 = \324)

3. A pair of blue jeans costs \$29.99 in Los Angeles. How much would this item cost in Canadian dollars if the exchange rate was \$1.00 Canadian = \$0.76 U.S.? ($29.99 \div .076 = \$39.46$ Canadian) **OL**

S Skill Practice

Using Line Graphs

Ask: According to the graph, which country's currency is more undervalued—Mexico or Japan? (Japan) Which three areas shown on the graph have currencies that are currently overvalued? (Euro area, Sweden, and Switzerland) **BL**

W Writing Support

Expository Writing Have students review the information in the text about the use of a gold standard. Direct them to write a paragraph that explains the concept of a gold standard and details how the United States stopped using this practice. Students should also explain why this change proved upsetting to many foreign governments. **OL**

The Global Economy & YOU

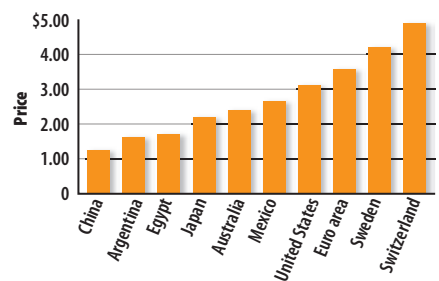


The Big Mac Index

Exchange rates should adjust to even out the cost of a market basket of goods and services, wherever it is bought around the world. For example, if you use Canadian dollars to buy a sandwich at a Tim Horton's restaurant in Canada, it should cost the same as if you bought the same sandwich using U.S. dollars at a Tim Horton's in the United States.

One way to see whether a currency is devalued or overvalued against the U.S. dollar is to use the "Big Mac Index" developed by *The Economist* magazine. Economists compare the price of a Big Mac hamburger in the United States to what it costs in another country's local currency. Converting the foreign price to U.S. dollars shows whether the price of a Big Mac is undervalued or overvalued against the U.S. dollar. The cheapest burger in the chart here is in China,

BIG MAC INDEX



Source: *The Economist*, using McDonald's price data

where it costs \$1.30, compared with an average American price of \$3.15. This implies that China's currency, the yuan, is 59 percent undervalued.

flexible exchange rates or floating exchange rates system that relies on supply and demand to determine the value of one currency in terms of another

which the price of one currency is fixed in terms of another currency so that the rate does not change.

Fixed exchange rates were popular when the world was on a gold standard. Gold served as the common denominator that allowed comparisons of currencies, and it kept exchange rates in line. For example, suppose that a country allowed its money supply to grow too fast and that some of the money was spent on imports. Under a gold standard, the countries receiving the currency had the right to demand that it be converted into gold. Because no country wanted to lose its gold, each country worked to keep its money supply from growing too fast.

This practice worked until the early 1960s when the United States developed a huge appetite for imports. During that time, American consumers bought large quantities of foreign goods with dollars. At first, foreign countries willingly held U.S. dollars because the dollars were acceptable throughout the world as an international currency. This meant that only a portion of

these dollars came back when other countries bought American exports.

As dollars began to pile up in the rest of the world, many countries wondered if the United States could honor its promise that the dollar was "as good as gold." Eventually several countries started redeeming their dollars, which drained U.S. gold reserves. As a result, President Richard Nixon announced in 1971 that the United States would no longer redeem foreign-held dollars for gold. This action saved the gold stock, but it also angered many foreign governments that had been planning on cashing their American dollars into gold.

Flexible Exchange Rates

As soon as the United States stopped redeeming foreign-held dollars for gold, the world monetary system shifted to a floating, or flexible, rate system. Under **flexible exchange rates**, also known as **floating exchange rates**, the forces of supply and demand establish the value of one country's currency in terms of another country's currency.

Differentiated Instruction

Working With Foreign Exchange Rates

Objective: Make calculations using foreign exchange rates.

Focus: Make sure that students understand what the values in each column of Figure 18.2 represent.

Teach: Have students answer the activity questions.

Assess: Call on students to share their answers. Discuss any incorrect answers as a class.

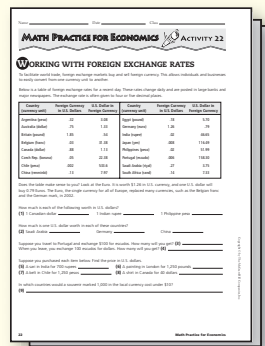
Close: Have students write a paragraph comparing and contrasting the values of international currencies.

Differentiated Instruction Strategies

BL Have students research and then draw pictures of three different foreign currencies.

AL Have students redo the activity with 10 nations not included in the table.

ELL **Ask:** Which other nations listed in the activity use the dollar as their basic currency unit? (Australia and Canada)



R Reading Strategy

Reading Graphs Ask: In what year did the trade-weighted value of the dollar peak? (1985) How would you describe the change of this value over the time period shown on the graph? (Possible answer: The trade-weighted value of the dollar generally seems to gradually rise and fall over the course of several years throughout the time period shown on the graph.) **BL**

D Differentiated Instruction

Verbal/Linguistic Request that verbal/linguistic learners practice explaining to the class the definitions of important concepts such as *trade deficit* and *trade surplus*. Further, invite these learners to describe in their own words the relationship between these concepts and the international value of a nation's currency. **OL**

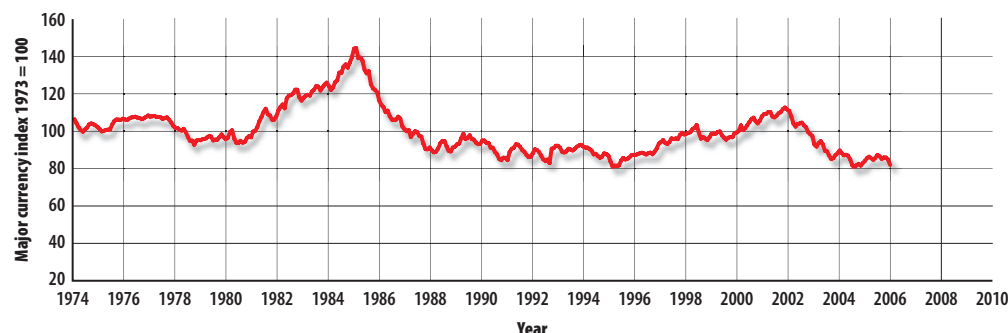
Economic Analysis

Answer: Imports become more expensive for Americans.

▶ The forces of supply and demand help set the international value of the dollar. Because the United States now imports more than it exports, the international value of the dollar has fallen.

Economic Analysis What happens to the cost of imports when the dollar falls?

MAJOR CURRENCY INDEX



Source: Federal Reserve System

trade deficit
balance of payments outcome when spending on imports exceeds revenues received from exports

trade surplus
balance of payments outcome when revenues received from exports exceed spending on imports

trade-weighted value of the dollar index showing strength of the U.S. dollar against a group of major foreign currencies

Trade Deficits and Surpluses

MAIN Idea The strength of the dollar affects trade and therefore trade deficits and surpluses.

Economics and You Have you ever bought an imported product because it was cheaper than the domestic alternative? Read on to find out how the changing value of the dollar affects the cost of goods.

A country has a **trade deficit** whenever the value of the products it imports exceeds the value of the products it exports. It has a **trade surplus** whenever the value of its exports exceeds the value of its imports. Each is dependent on the international value of its currency.

International Value of the Dollar

Since the dollar started to float in 1971, the Fed has kept a statistic that measures the strength of the dollar. **Figure 16.6** shows the **trade-weighted value of the dollar**, an

index displaying the strength of the dollar against a group of major foreign currencies. When the index falls, the dollar is weak in relation to other currencies. When the index rises, the dollar is strong.

When the dollar is strong, as it was in 1985 and 2002, foreign goods become less costly and American exports become more costly for the rest of the world. As a result, imports rise, exports fall, and trade deficits result. With more dollars going abroad, the value of the dollar then goes down.

Effect of a Trade Deficit

A **persistent** trade imbalance can cause a chain reaction that affects income and employment. To illustrate, the large U.S. trade deficit in 2005 and 2006 flooded the foreign exchange markets with dollars. The increase in the supply of dollars on world markets caused the dollar to lose some of its value, making imports more expensive for Americans and exports less expensive for foreigners.

Hands-On Chapter Project

Step 3

Analyzing World Trade

Step 3: Studying Exchange Rates and Balance of Trade. Student groups will identify currency exchange rates and the U.S. trade balance with specific nations.

Directions: Organize the class into the same five groups that were formed for Step 1. Tell groups to imagine that they run "international" stores that take many different currencies. Tell groups to assign

one retailing area (for example, clothing, groceries, electrical appliances, and so on) to each of its students. Students should then investigate the prices charged at local stores for five items in their assigned retailing area. Then have students use the exchange rate table in a newspaper business section to find equivalent prices in the currencies of at least three nations on the continent assigned to their group in Step 1. Students may select the same nations as other members of their group.

Direct groups to combine their findings to create price billboards showing items, countries, and prices.

Assessing Have groups research the current U.S. balance of trade with the nations they studied. Then ask each group to write a short paper assessing how exchange rates may have affected the nation's trade with the United States. **OL**

(Chapter Project continued in Visual Summary.)

The recent trade imbalance provided some relief to the U.S. automobile industry. A weaker dollar drives up the price of Japanese-built cars relative to American-built ones. As a result, imported automobiles becomes less attractive to American buyers. If the dollar continues to weaken, other domestic industries will be affected in a similar manner.

When the value of the dollar gets low enough, the process will reverse. Foreigners will sell their currency so that they can buy more American products. This will drive the value of the dollar up, making it more difficult for American export industries and easier for import industries.

A Strong vs. a Weak Dollar

Changes in the international supply and demand for dollars cause the value of the dollar to change daily. What is best—a strong dollar or a weak dollar?

The answer is: neither. Under flexible exchange rates, trade deficits tend to correct themselves automatically through the price system. A strong currency generally

Did You Know?

► **Duty-Free** When Americans return from traveling abroad, they have to fill out a customs declaration form that lists the dollar value of goods they purchased during their trips. Travelers can bring home items ranging in value from \$200 to \$800 duty-free. For anything over that amount, customs officials will charge a duty, or tax on imports. The original purpose of this customs law was to help the balance of payments by making it more difficult for Americans to shop abroad—which shows up as an “import” in the balance of payments accounts.

leads to a deficit in the balance of goods and services and a subsequent decline in the value of the currency. A weak currency tends to cause a trade surplus, which eventually pulls up the value of the currency.

Because one sector of the economy is hurt while another is helped, there is no net gain in having either a strong or a weak dollar. As a result, the United States and many other countries no longer design economic policies just to improve the strength of their currency on international markets.

✓ **Reading Check** **Describing** Why did the value of the dollar fall in 2005 and 2006?

SECTION

3

Review

Vocabulary

- 1. Explain** the significance of foreign exchange, foreign exchange rate, fixed exchange rates, flexible exchange rates, floating exchange rates, trade deficit, trade surplus, and trade-weighted value of the dollar.

Main Ideas

- 2. Identifying** What are the factors involved in determining exchange rates?
- 3. Describing** Use a graphic organizer like the one below to describe what is meant by a strong or weak dollar, and how each affects the prices of imports and exports.

	Description	Effect on imports	Effect on exports
Strong dollar			
Weak dollar			

Critical Thinking

- 4. The BIG Idea** What is the relationship between foreign trade and the international value of the dollar?
- 5. Making Generalizations** What would happen if the United States lost its comparative advantage in producing soybeans?
- 6. Analyzing Visuals** Use the information from Figure 16.4 on page 457 to compare the price of a pair of \$100 tennis shoes in the United States with the same brand sold (a) in South Korea at 11,000 ₩ (won) and (b) in France for 100€ (euros).

Applying Economics

- 7. Exchange Rates** You are planning to travel to Canada in the next week and have just learned that the Canadian dollar has weakened. Is this good news or bad news? Explain your answer.

C Critical Thinking

Synthesizing Ask: Why might many countries have decided against designing economic policies in order to improve the international strength of their currencies? (These countries may have decided against this practice because doing so often benefits one sector of a nation's economy, while having a negative impact on other sectors of the economy.) **OL**

✓ **Reading Check** **Answer:** because a large U.S. trade deficit flooded the foreign exchange markets with dollars

Assess

Use the Interactive Tutor Self-Assessment CD-ROM to review Section 3, and then assign the Section 3 Review as homework or as an in-class activity.

Close

Making Connections Have students write a short response detailing how a change in the value of the dollar might affect their daily lives. **OL**

Review

SECTION

3

Answers

- All definitions can be found in the section and the Glossary.
- supply and demand for a nation's currency in relation to another nation's currency
- Strong dollar:** dollar has increased in value in relation to other currencies; Effect on imports—less expensive for U.S. buyers, imports increase; Effect on exports—more expensive for foreign buyers, exports decrease. **Weak dollar:** dollar has decreased in value in relation to other currencies; Effect on imports—more expensive for U.S. buyers, imports decrease; Effect on exports—less expensive for foreign buyers, exports increase
- When the value of the dollar increases, imports increase because they are relatively cheaper and exports decrease because they are more expensive. When the value of the dollar decreases, the reverse occurs.
- If the dollar rises, U.S. farmers will be less able to sell their products abroad because soybeans from other sources would be relatively cheaper to produce.
- In South Korea, the shoes would sell for the equivalent of \$11.79. In France, the shoes would sell for the equivalent of \$128.88.
- Students should recognize that this is good news because U.S. dollars will now have an increased value in Canada, meaning that the purchasing power has increased.

Teach

W Writing Support

Personal Writing Tell students to suppose that a business planner from a company such as Yahoo! has asked them to share their ideas about ways that they would like to see Internet technologies improve in the future. Direct students to write a brief personal essay in which they share their views on this subject. Remind students that in a personal essay they may choose to support their opinions with facts and observations from their own experience. **OL**

Examining the Profile

Answers:

1. Yang began partly to do research for his doctoral thesis and partly to find information about his fantasy basketball league.
2. by finding new ways to build the audience for Yahoo! and by seeking input from current users

Additional Support

Profiles **in** Economics



Jerry Yang, along with his partner David Filo, built a search engine in a trailer at Stanford University to help with their research—and to have some fun. Soon “people from all over the world were using this database that we created.”

Jerry Yang (1968–)

- cofounder of the Internet Web portal Yahoo!
- became a billionaire three years after starting the company
- ranked on *Forbes*’s list of the world’s richest people

Yahoo! . . . and Having Fun

When 10-year-old Jerry Yang immigrated to the United States from Taiwan, getting an advanced degree was a distant dream. But in 1994, he found himself working on his Ph.D. at Stanford University. Along with his friend David Filo, he began searching sites on the Internet, partly to do research for their doctoral theses . . . and partly to find information about their fantasy basketball leagues.

Frustrated by the chaos of information on the Web, the two students began to organize sites into subject-based categories. Soon the online traffic flocking to “Jerry’s Guide to the World Wide Web” caught the attention of venture capitalists, who provided funds for the start-up company in 1995. Yang and Filo renamed their site Yahoo!, short for “Yet Another Hierarchical Official Oracle,” and called themselves “Chief Yahoos.”

The Face of Business

Yang has become the public face and business mind of Yahoo!, but he does not direct the day-to-day operations of the company. Instead, he helps develop business strategy and future business direction. Constant travel brings him to all parts of the world, where he can see firsthand how people use his search engine. This helps him with ideas for growing and expanding Yahoo!.

W Yang wants to stay on the cutting edge of Web development, and he wants “to continue to get audience.” He knows his site is a hub for online groups worldwide. One way he plans to expand his audience is by tapping into these user groups to find out what they want. Yang also does not hesitate to move away from the Web and develop information delivery on cell phones and other tools.

Despite all this success, Yang has not quite given up on his educational dream. Even today, the Yahoo media relations site lists him as “currently on a leave of absence from Stanford’s electrical engineering Ph.D. program.”

Examining the Profile

1. **Summarizing** Why did Yang begin organizing Internet sites?
2. **Analyzing** How does Yang hope to stay ahead of the competition?

Extending the Content

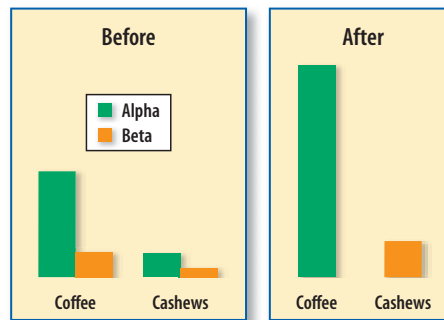
About Yahoo! Founded in 1994, Yahoo! has become one of the most popular search engines on the World Wide Web. The site now offers a variety of specialized search options that allow users to locate sites related to news, shopping, video, and images. In addition to its utility as a search engine, Yahoo! also provides e-mail, instant messaging, and other communication services to users. Further, Yahoo! has

partnered with numerous media providers to offer users access to content in a variety of fields, such as entertainment, sports, and finance. Yahoo! is based in Sunnyvale, California, but now has offices around the world.

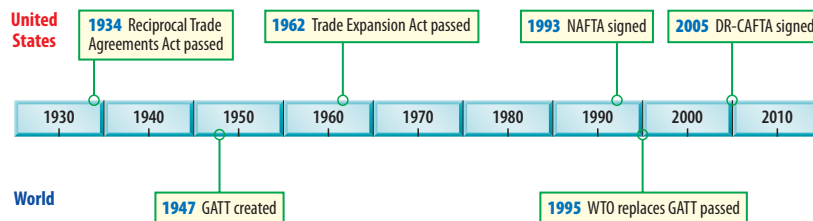


Study anywhere, anytime!
Download quizzes and flash cards to your
PDA from glencoe.com.

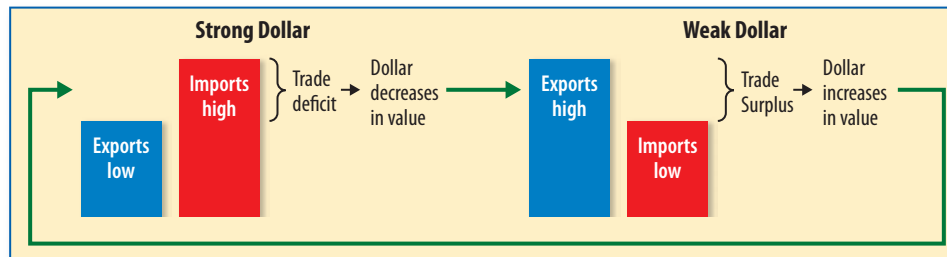
- ▶ **Absolute and Comparative Advantage** A country has absolute advantage when it can produce more of a product than can another country. It has comparative advantage when it can produce a product at a lower opportunity cost than another country. When countries focus on those products for which they have comparative advantage, world production increases.



- ▶ **Free Trade Movement** After strict tariffs severely limited world trade during the early years of the Great Depression, the United States and other countries worked to open trade.



- ▶ **Trade Deficits and Surpluses** The strength of the dollar affects the balance of trade of the United States.



Assessing Ask students to think about the factors that might give one country an absolute advantage over another country. Then have them contrast these factors with those that might give a country a comparative advantage. **Ask:** What process has taken place between the graphs labeled “Before” and “After”? Which country holds a comparative advantage in which product? (Specialization has taken place between the “Before” and “After” graphs. Country Alpha holds a comparative advantage in coffee, while Country Beta holds a comparative advantage in cashews.) **BL**

Speculating Direct students to review the information presented in the time line. Then ask them to write a brief essay in which they speculate on the reasons for the increasing openness of international trade throughout the twentieth century and into the present. Students should use information from the time line, as well as the chapter text, to support their speculations. Invite students to share their responses with the class. **OL**

Analyzing World Trade

Step 4: Complete the Analysis. Student teams will summarize what they learned in Steps 1–3.

Directions: Write the Big Idea for this chapter on the board. Have students write an essay elaborating on how trade and specialization have promoted economic growth in the nations on the continent assigned to their

group. Students will work alone on this activity—each student will write his or her own essay. Students should integrate into their essays concepts that they learned from each of the previous steps of this chapter project. Ask volunteers to read their essays to the class. Discuss as a class the ideas brought up by students’ essays. **OL**

Hands-On Chapter Project

Step 4: Wrap Up

ExamView®

Assessment Suite

This easy-to-use software includes extensive question banks and allows you to create fully customized tests that can be administered in print or online.

Review Content Vocabulary

- 1.–12. Clues should demonstrate a clear understanding of the terms in an economic context.

Review Academic Vocabulary

13. f 14. a
15. b 16. c
17. e 18. d

Review the Main Ideas

19. Everyone will be better off producing the products they produce relatively best.
20. It allows countries to trade the things that they produce best in exchange for the resources they otherwise lack.
21. It raises the total world output and standard of living.
22. Protective tariff: places a high tax on imports in order to protect less-efficient domestic industries. Revenue tariff: high enough to generate revenue for a government without prohibiting imports.
23. by preventing American industries from being undersold by foreign companies
24. **Possible answer:** WTO: international agency that administers trade agreements signed under GATT; settles trade disputes, organizes trade negotiations;

Review Content Vocabulary

Write crossword puzzle clues for the terms below. All clues should relate to the content of this chapter and should differ from the definitions in the textbook. Create a puzzle grid as an additional challenge.

- absolute advantage
- balance of payments
- comparative advantage
- foreign exchange rate
- exports
- trade surplus
- imports
- protectionism
- quota
- tariff
- trade deficit
- flexible exchange rate

Review Academic Vocabulary

Match each term below with its synonym.

- a. enable
b. imposed
c. justify
d. persistent
e. secure
f. volume
13. capacity, amount, quantity
14. facilitate, permit, make possible
15. forced, established, ordered
16. defend, excuse, rationalize
17. gain, acquire, access
18. tenacious, enduring, constant

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assists and trains developing countries. NAFTA: agreement to liberalize free trade among the United States, Canada, and Mexico; plans to phase out trade restrictions among the members

25. Supply and demand establishes the value in terms of another country's currency.

26. Meaning: a country's spending on imports exceeds revenues received from its exports. Effect: the dollar loses some of its value, making imports more expensive and exports less expensive.

Review the Main Ideas

Section 1 (pages 441–445)

19. **Identify** the basic assumption supporting the theory of comparative advantage.
20. **Explain** how comparative advantage helps nations acquire goods, services, and the resources they otherwise lack.
21. **Explain** why international trade is important in today's economy.

Section 2 (pages 447–454)

22. **Describe** the different types of tariffs.
23. **Explain** how tariffs and quotas protect American jobs.
24. **Describe** two attempts to facilitate the growth of international trade by using a graphic organizer like the one below.

Agreement or Organization	Description	Encourages trade by...

Section 3 (pages 456–461)

25. **Describe** how the value of the dollar is established using a flexible exchange rate.
26. **Describe** the meaning and effect of a trade deficit.
27. **Identify** the reason why the United States switched to a flexible exchange-rate system in the early 1970s.

Critical Thinking

28. **The BIG Idea** Why is a nation with abundant resources better off trading than being self-sufficient?
29. **Synthesizing** How does comparative advantage make trade between countries of different sizes possible?
30. **Drawing Conclusions** Do you favor protectionism as a national trade policy? Why or why not?

27. because nations tried to redeem dollars for gold, which drained the gold supply

Critical Thinking

28. Being self-sufficient will result in a lower standard of living than would be possible with specialization and trade.
29. Students should note that the efficient use of resources is most important.
30. Answers will vary but should demonstrate an understanding of protectionism.

- 31. Making Inferences** How might the issue of protectionism differ for a worker and a consumer? Use examples to support your argument.
- 32. Analyzing Information** Some people think the United States should return to a system of fixed exchange rates. Defend or oppose this view. Cite examples to support your position.
- 33. Drawing Conclusions** How do trade deficits correct themselves under a system of flexible exchange rates?
- 34. Synthesizing Information** Why do you need to know the exchange rate when you plan a trip to a foreign country?

Math Practice

- 35. Imagine** that you are traveling through South America and staying in budget hotels. Based on the average room rates and exchange rates in the table below, establish the room rates in dollars for each country.

Country	Cost of room in foreign currency	Currency per U.S. \$	Cost of room in U.S. \$
Argentina (peso)	70	0.3247	
Bolivia (boliviano)	96	0.1251	
Brazil (real)	71	0.4561	
Chile (peso)	80	0.001853	
Paraguay (guarani)	41,100	0.0001826	
Peru (nuevo sol)	49	0.3086	
Uruguay (new peso)	299	0.04185	
Venezuela (bolivar)	35,000	0.0003818	

Thinking Like an Economist

- 36.** Assume that the United States is running a large trade deficit. What predictions would you make about future changes in the value of the dollar in foreign exchange markets? Would these developments be a matter of concern? Explain your answer.

Writing About Economics

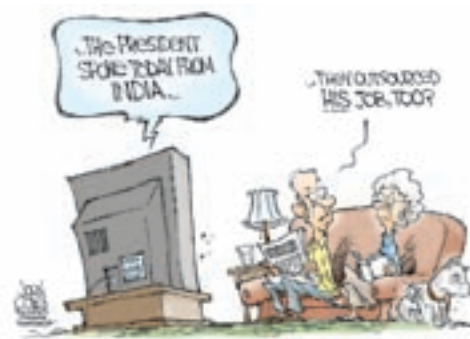
- 37. Persuasive Writing** During the course of one day, make a list of at least 10 manufactured items that you handle, such as your clothing and the cafeteria trays used in your school. Find out where each item is produced, and make a log of the items, noting whether each is domestic- or foreign-made. Based on your log and the information in this chapter, write a persuasive essay supporting or opposing international trade.

Applying Economic Concepts

- 38. Foreign Exchange** How does a weak U.S. dollar affect you as a consumer? How does a strong dollar affect you? Explain.
- 39. Comparative Advantage** Think of a project you recently completed with a friend. Apply the principle of comparative advantage to the way you and your friend worked. How could you have completed the project more efficiently? Explain.

Interpreting Cartoons

- 40. Critical Thinking** What aspect of foreign trade does the cartoonist illustrate in this cartoon? Do you think the cartoon is effective? Explain.



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- 31.** Workers in a threatened industry will likely support protectionists because they do not want to lose their jobs. Consumers tend to oppose protectionism because trade barriers generally lead to higher prices. Examples will vary.
- 32.** Students should present their arguments using supporting details from the text.
- 33.** A persistent trade deficit tends to reduce the value of a country's currency. In other words, supply of currency exceeds demand. This, in turn, makes imports cost more and exports cost less. Over time,

foreigners will sell their currency to acquire U.S. dollars so they can buy the cheaper U.S. goods. Supply and demand move toward equilibrium, and the trade deficit declines.

- 34.** Since other countries do not use the U.S. dollar as their currency, you need to know how much your dollars are worth and what your spending power will be. You can plan your trip more effectively and stay within your trip budget if you are aware of the exchange rates.

Economics ONLINE

Have students visit the Web site at glencoe.com to review Chapter 16 and take the **Self-Check Quiz**.

Math Practice

- 35.** Argentina—\$22.73
Bolivia—\$12.01
Brazil—\$32.38
Chile—\$0.15
Paraguay—\$7.50
Peru—\$15.12
Uruguay—\$12.51
Venezuela—\$13.36

Thinking Like an Economist

- 36.** Answers should demonstrate understanding of foreign exchange markets and be supported by sound economic reasoning.

Writing About Economics

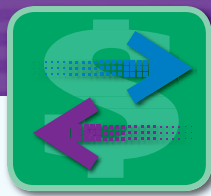
- 37.** Answers will vary but should address the issue of international trade.

Applying Economic Concepts

- 38.** A weak dollar means that consumers will pay more for any imported good or for products made with imported parts/resources. With a strong dollar, consumers will pay less for the imported items.
- 39.** Answers will vary but should demonstrate an understanding of comparative advantage.

Interpreting Cartoons

- 40.** The cartoonist points out that one of the potential costs of international trade is the loss of domestic jobs. Students' assessments of the cartoon will vary.



Will CAFTA Be Beneficial to the U.S.?

Focus

Ask students to use a map to locate Costa Rica, the Dominican Republic, El Salvador, Guatemala, Honduras, and Nicaragua. Have students discuss why these nations might make good trading partners with the United States. *(Possible answer: They are located near the United States, and these nations and the United States would possess different resources that could benefit one another.)*

Teach

R Reading Strategy

Reading Charts Ask: **What category of U.S. imports is subject to the highest tariff?** *(motor vehicles/parts)* **What conclusions can you draw about why this might be the case?** *(Possible answer: This may be because the nations want to establish a similar industry in their region but cannot yet directly compete with American automakers.)* **OL**

Additional Support

As you learned in Chapter 1, the United States has a remarkable degree of economic interdependence with other nations. On August 2, 2005, President George W. Bush expanded this interdependence by signing into law DR-CAFTA—the Dominican Republic-Central America Free Trade Agreement. This agreement among the United States and Costa Rica, the Dominican Republic, El Salvador, Guatemala, Honduras, and Nicaragua takes effect as soon as all countries involved ratify it. Still, it was hotly debated. Some believe the agreement, sometimes called CAFTA, will help the U.S. economy. Others fear it will be harmful.

Who is right? As you read the selections, ask yourself: Will DR-CAFTA help or harm the U.S. economy?

PRO CAFTA: A WIN-WIN CASE

The economic case for CAFTA is compelling. First, the level playing field created by the pact would benefit U.S. consumers and businesses. Currently about 80% of Central American products enter the U.S. duty-free. CAFTA would provide some balance with reciprocal treatment for U.S. goods and agricultural exports, and all tariffs on U.S. goods would be eliminated over time. CAFTA would also require increased transparency in corporate governance, legal systems, and due process in the region, strengthening the local economies. For U.S. business, the newly expanded access to the region would benefit companies in financial services, telecommunications, entertainment, and computer services. CAFTA, moreover, would create jobs in Central America and make the region's economies more competitive with Asian nations.

... There are foreign policy reasons to favor the CAFTA accord. Since the 1970s, CAFTA nations have moved toward market economies and democracy, becoming commercial and political allies of the U.S. CAFTA's boost to economic growth and incomes in Central America would further bolster support for free markets and democratic institutions.

—Glenn Hubbard, Dean of the
Columbia University Business School

CAFTA-DR eliminates these tariffs:

- El Salvador's 30% auto tariff
- Guatemala's 23% tariff on certain footwear
- Plastics and cosmetics tariff of up to 15%
- Air conditioning and refrigeration equipment tariffs of up to 15%
- Building products and home construction accessories, including fixtures, sinks, and doors, 15% tariffs

Current Tariffs on Central America and Dominican Republic Imports from the U.S.

Motor vehicles/parts	11.0%
Wood products	10.0%
Textile/apparel/leather products	10.0%
Chemicals/petroleum/coal/rubber	5.0%
Ferrous metals	6.3%
Other metals/metal products	3.5%
Transport equipment	3.5%
Electronic equipment	1.4%
Other machinery/equipment	4.0%
Other manufactures	7.1%

Source: www.export.gov

Extending the Content

About CAFTA The U.S. Congress approved the Dominican Republic-Central America Free Trade Agreement, or CAFTA, in July of 2005. President George W. Bush signed the agreement into law on August 2, 2005. The legislature of the Dominican Republic, as well as those of El Salvador, Guatemala, Honduras, and Nicaragua, has ratified CAFTA. Such ratification is currently pending in Costa Rica. Because different countries have approved the

agreement at different times, the United States has chosen to enact the legislation in each country as the nation takes the necessary steps to comply with CAFTA. The first country to do so was El Salvador, in March of 2006. The nations of CAFTA have become an increasingly important destination for U.S. exports in recent years. These countries represent the tenth largest U.S. export market in the world, ahead of nations such as Russia and India.



Assess/ Close

W Writing Support

Expository Writing Direct students to use library and Internet resources to research the impact of NAFTA on employment in their home state. Then have students write a brief essay describing their findings. **AL**

Analyzing the Issue

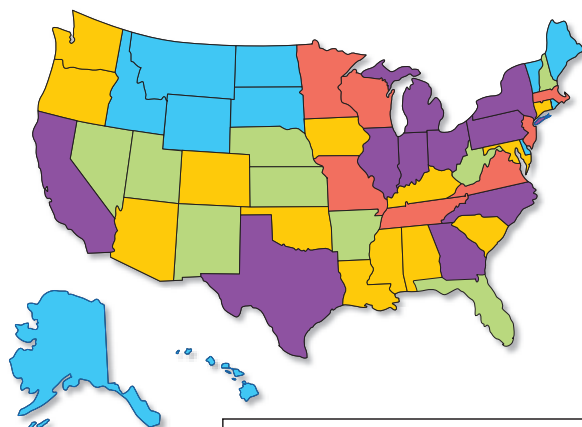
Answers:

1. would provide a more balanced treatment of U.S. goods and agricultural exports; would lead to better corporate governance; would give U.S. businesses greater access to these countries, while strengthening each nation
2. They believe that CAFTA will not institute labor or environmental standards.
3. Answers will vary but should be logical and well supported.

Additional Support

CON CAFTA COULD LEAD TO FURTHER U.S. JOB DISPLACEMENT

NAFTA COSTS JOBS IN EVERY STATE



Source:
REPI analysis of Bureau of Labor
Statistics and Census Bureau data.

No protections were contained in [NAFTA] to maintain labor or environmental standards. As a result, NAFTA tilted the economic playing field in favor of investors and against workers and the environment, causing a hemispheric "race to the bottom" in wages and environmental quality.

... These experiences raise serious questions about the likely economic impact of the ... DR-CAFTA agreement on the economies of the United States, and equally important, its neighbors in the Dominican Republic and Central America.

—Robert E. Scott, Director of International Programs, Economic Policy Institute, and David Ratner, research assistant at the Economic Policy Institute

Analyzing the Issue

1. **Identifying** What arguments does Hubbard make in support of DR-CAFTA?
2. **Summarizing** Why do Scott and Ratner believe DR-CAFTA will not benefit either the United States or Central America?
3. **Deciding** Which opinion do you believe is correct? Explain your reasoning.

Activity: Technology Connection

Plan a Web Site Organize the class into small groups. Instruct students in each group to conduct Internet research to find Web sites that both support and oppose the Dominican Republic-Central America Free Trade Agreement. Ask students to study these Web sites and identify the components that the designers have

included, such as text, graphics, photos, and so on.

After students have studied several of these Web sites, direct each group to choose one side of the debate and then plan their own Web site for this position. Remind groups to consider which elements they found most

compelling and convincing during their study of the other CAFTA Web sites. Have group members work together to select what elements they will include and then sketch out a plan for the design of the Web site and its contents. Invite each group to present their Web site plans to the class. **OL**