UNIT – IV

International trade and the WTO

Comparative cost · Heckscher–Ohlin · Terms of trade · WTO

Explanatory Lecture Slides

Money, Banking & International Trade · Major-2 · Semester II

MONEY, BANKING & INTERNATIONAL TRADE

LEARNING OBJECTIVES

Topics covered in this unit

01 State the comparative-cost theory and criticise it

02 Explain Heckscher–Ohlin in one page

03 Define terms of trade and its types

04 State WTO structure, objectives, functions

05 Place tariffs, quotas and FDI

06 Name the Indian legal face (Customs, FEMA, FTAs)

How this unit is organised

01	02	03	04	05	06
Comparative cost	Criticism	Heckscher–Ohlin	Terms of trade	WTO	Tariffs & FDI

Comparative-cost theory — Ricardo

Even if Portugal is better at both wine and cloth, trade pays if opportunity costs differ. Specialise where the relative cost is lower.

- Absolute cost (Smith) is not required.
- PYQ: critically examine comparative-cost theory (2021, 2022, 2025).
- Assumptions: two countries two goods, labour theory, no transport cost, full employment, free trade.
- Criticism: labour is not the only factor; transport exists; infant industry (List/Hamilton); unequal exchange.

Comparative-cost theory — Ricardo

CORE

- Relative, not absolute, cost.

ATTACK

- Unrealistic assumptions.
- Static.
- Ignores power and colonies.

Heckscher–Ohlin

A country exports goods that use its abundant factor intensively. Factor endowments, not only labour time.

- PYQ: Heckscher–Ohlin (2023).
- Leontief paradox as criticism (US exports labour-intensive?).
- Useful one-line: relative factor abundance explains trade pattern.

Heckscher–Ohlin

PREDICTS

- Labour-rich country exports labour-intensive goods.

LIMITS

- Technology gaps.
- Demand differences.
- Intra-industry trade.

Terms of trade

The rate at which exports exchange for imports. Net barter TOT = Px / Pm × 100.

- Gross barter, income TOT, factorial TOT — PYQ ‘different concepts of terms of trade’ (2023, 2022).
- A deterioration means more exports for the same imports — a development issue for India.
- Prebisch–Singer: primary-product TOT tend to fall — one line.

Terms of trade

NET BARTER

- Export-price index / import-price index.

WHY IT MOVES

- Demand.
- Elasticity.
- Tariffs.
- Exchange rate.

WTO — structure and functions

Born 1995 from GATT 1947. Legal institution with a dispute-settlement body.

- PYQ: objectives and functions of WTO; structure (2021, 2022, 2023 Oct).
- Pillars: GATT (goods), GATS (services), TRIPS (IP).
- Principles: MFN, national treatment, tariff binding, transparency.
- Ministerial Conference, General Council, DSB, Secretariat at Geneva.
- India is a founding member — mention once.

WTO — structure and functions

OBJECTIVES

- Raise living standards.
- Full employment.
- Expand trade.
- Sustainable development (preamble).

FUNCTIONS

- Implement agreements.
- Forum for negotiation.
- DSB.
- Coherence with IMF/World Bank.

Tariffs, quotas, FDI

PYQ short notes: tariffs and quotas; FDI (2023).

- Tariff: a tax on imports (Customs Tariff Act).
- Quota: a quantity cap — often more distorting; quantitative restrictions were a GATT/WTO fight India lost in part (QRs, 2001).
- FDI: capital that stays; FEMA 1999 + sectoral caps + DPIIT policy; not FPI.
- Infant-industry case for protection; rent-seeking case against it.

Tariffs, quotas, FDI

TARIFF

- Price instrument.
- Revenue.

QUOTA

- Quantity instrument.
- Windfall to licence-holders.

Balance of payments — a teaser for Unit V

A systematic record of all economic transactions of residents with the rest of the world.

- Current account (goods, services, transfers) + capital account.
- PYQ: BOP disequilibrium causes (2023).
- A deficit is not a sin; a persistent one financed by unstable flows is.

Balance of payments — a teaser for Unit V

CURRENT

- Trade.
- Invisibles.
- Transfers.

CAPITAL

- FDI, FPI, loans, banking capital.

WTO — structure and functions

Born 1995 from GATT 1947. Legal institution with a dispute-settlement body.

- PYQ: objectives and functions of WTO; structure (2021, 2022, 2023 Oct).
- Pillars: GATT (goods), GATS (services), TRIPS (IP).
- Principles: MFN, national treatment, tariff binding, transparency.
- Ministerial Conference, General Council, DSB, Secretariat at Geneva.
- India is a founding member — mention once.

LANDMARK AUTHORITIES

Cases a KSLU answer should name

CASE

India — Quantitative Restrictions (WTO)

DS90 / 2001 context

WTO law constrained India's QRs — comparative cost meets a treaty.

CASE

Novartis AG v Union of India

(2013) 6 SCC 1

TRIPS-plus pressure v Patents Act s.3(d) — WTO is not a repeal of parliamentary space.

CASE

Jeevan Ltd-type customs valuation cases

use Customs Act ss.14 if needed

Tariff without valuation rules is an empty tax.

STATUTE / SECTION MAP

Provisions & materials to quote

Customs Act 1962 / Tar	The Indian face of a tariff.
FEMA 1999	Current v capital account; FDI routing.
Patents Act / TRIPS	IP as a trade obligation.
FTDR Act 1992	Export-import policy’s parent.
WTO Agreement 1994	Treaty source; implemented by statutes, not by a WTO policeman in Delhi.

WRITE IT IN THE HALL

10 / 16-mark frames from this unit

Q1 Critically examine the comparative-cost theory of international trade.

Q2 Discuss the Heckscher–Ohlin theory.

Q3 State the terms of trade. Explain different concepts.

Q4 Explain the structure, objectives and functions of the WTO.

BEFORE YOU CLOSE THE FILE

Unit recap

1. Ricardo: relative cost, not absolute.
2. H–O: factor endowments.
3. TOT = export prices over import prices (net barter).
4. WTO = GATT + GATS + TRIPS + DSB.
5. Tariff taxes; quota rations; FDI is capital that stays.