Date ___/___/______ Page No.: (1)

Date – 20/04/2020	Degree Part – II (Hons.)
Content Writer:–	Paper :– IV
Dr. Abhay Kumar Pathak	Content of the Paper:
Dept. of ECONOMICS,	International Economics
Marwari College,	Module – 2
Darbhanga (LNMU)	

TOPIC :– ANALYSIS OF GAINS FROM TRADE

International trade is done because it is gainful to the trading countries. Gains from trade are of various nature. They are as follows:-

(I) International trade involves territorial division of labour and regional specialisation in production. This leads to increased productivity, ~~thus~~, low cost and more output.

(II) Trade leads to capital utilisation of the trading country's resources.

(III) A country can get goods which it can not itself produce due to lack of technical knowledge and other reasons.

(IV) It promotes competition, economic alertness and efficiency in the country.

(V) It makes it possible to have consumption of more varities and improvements in world's welfare at large.

(VI) Trade leads to expansion of the size of market, thereby leading to more and more complex division of labour and improvement in productivity.

In analysis of classical theory of international trade, specialisation based on the principle of comparative cost advantage is the major source of gain from international trade. An additional source is the possibility of exploiting economies of scale when the size of the market expands through the foreign trade of a country.

Distribution of Gains :-

Sharing of gains from international trade primarily depends on the terms of trade. If a country has favourable terms of trade, it will claim a larger share in the distribution of gains. Therefore, the distribution of gains from trade can be measured in following terms:-

(I) Terms of trade.
(II) Domestic cost ratios.

A country gets a larger share in proportion to its favourable terms of trade. Gain occurs when cost of production is reduced on account of specialisation process involved in trade. When a country's domestic cost of production and terms of trade are settled nearer to the opposite trading country's cost ratio, its share in the gains will tend to be larger.

Changes in Gains :-

Changes in gains may occur due to following reasons :-

(1) Changes in the terms of trade largely affects the gains when terms of trade of a country become favourable, its proportion of sharing in gains from trade becomes larger.
(2) Changes in the cost of production of exports of a country affects its gain. If due to technological advancement and other reasons, cost of production is reduced, the exporting country will find an improvement in its gain.

Date ___/___/______

(3) When the volume of trade of a country increases, its gains also increase.

(4) With changes in the composition of the pattern of trade, a country's gains also change. If a country's export change such that commodities with greater comparative cost advantage are replaced for goods with lower comparative costs advantage, its gains improve.

Types of Terms of Trade:-

The rate at which one country's products exchange for those of other is referred to as 'terms of trade'. The terms of trade expresses the relationship between the export price and import price of a country. Terms of trade may be favourable or unfavourable to a country. When the export price is greater than the import price, terms of trade are favourable to the country. If import price is greater than the export price, terms of trade are unfavourable to the country. Following are the major terms of trade :-

(1). Net Barter Terms of Trade:-

The ratio of price of export index to price of import index is referred to as net barter terms of trade.

In symbolic terms:-

$$NBTT = \frac{P_x}{P_m} \times 100$$

Where, NBTT = net barter terms of trade,

P_x = Price of export,

P_m = Price of imports.

Here, we can analyse that if $P_x > P_m$, terms of trade is favourable.

(II) <u>Gross Barter Terms of Trade</u>:-

The gross barter terms of trade is an index of relationship of the total physical quantity of exports. Symbolically, it may be written as:-

$$GBTT = \frac{Q_m}{Q_x} \times 100$$

where, GBTT = gross barter terms of trade,
Q_m = volume of physical quantity of imports,
Q_x = volume of exports.

If $Q_m > Q_x$, terms of trade is favourable.

(III) <u>Income Terms of Trade</u>:-

Income terms of trade is measured by multiplying volumes of exports with the net barter terms of trade.

Hence,

$$ITT = Q_x\left(\frac{P_x}{P_m}\right)$$

where, ITT = income terms of trade,
Q_x = volume of exports,
P_x = Price of exports,
P_m = Price of imports.