OCR Economics A-level

Macroeconomics

Topic 4 – The Global Context

Definitions and Concepts

4.1 – International trade

International trade - Exchange of goods and services between countries.

4.2 – Exchange rates

Bilateral exchange rates - The value of one currency expressed in another currency.

Effective exchange rates - Describes the strength of one currency to a basket of other currencies using an index.

Exchange rates - The purchasing power of a currency in terms of what it can buy of other currencies.

Fixed exchange rate - The value of the currency is set against the value of another and that exchange rate does not change.

Floating exchange rate - Value of the currency is determined purely by market demand and supply of the currency.

Hybrid exchange rate system - A combination of the characteristics of fixed and floating exchange rates; the currency fluctuates but it doesn't float on a fully free market e.g. managed float.

Nominal exchange rates - The weight of one currency relative to another, without being adjusted for inflation.

Real exchange rates - When the exchange rate is adjusted for inflation to give a more accurate reflection of purchasing power.

4.3 – Globalisation

Absolute advantage - When a country can produce a good more cheaply in absolute terms than another country.

Comparative advantage - When a country is able to produce a good more cheaply relative to other goods produced; it has a lower opportunity cost.

Globalisation - The growing interdependence of countries and the rapid rate of change it brings about; movement towards free trade of goods and services, free movement of labour and capital and free interchange of technology and intellectual capital.

International competitiveness - The ability of a country to compete effectively and become attractive in international markets.

J-Curve - A current account will worsen before it improves following a depreciation of the currency.

Marshall-Lerner condition - The sum of the price elasticities of imports and exports must be more than one if a currency depreciation is to have a positive impact on the trade balance.

Terms of trade - The ratio of an index of a country's export prices to an index of its import prices. Expressed by: (average export price index x100) / average import price index.

4.4 – Trade policies and negotiations

Customs union - The removal of all tariff barriers between members and the introduction of a common external tariff.

Economic union - A common market with a customs union and free movement of goods, services, capital and labour.

Embargoes - Complete ban on trade with a particular country.

Free trade - Trade with no barriers or restrictions.

Free trade areas - Where countries agree to trade goods with other members without protectionist barriers.

Monetary union - Two or more countries with a single currency.

Protectionism - When the government enact policies to restrict the free entry of imports into their country, such as tariffs and quotas.

Quotas - Limits placed on the level of imports allowed into a country.

Tariffs - Taxes placed on imported goods in an attempt to prevent people from buying them.

Trade creation - When a country moves from buying goods from a high cost to a lower cost producer.

Trade diversion - When a country moves from buying goods from a low cost producer to a higher cost one.