# 4.4 Economic integration

Level7 Education

# Learning objectives

| 4.4 Economic integration | Depth | Diagrams and calculations |
|---|---|---|
| Preferential trade agreements<br>• Bilateral<br>• Regional<br>• Multilateral (the World Trade Organization) | AO1 | |
| Trading blocs<br>• Free trade areas/agreements<br>• Customs unions<br>• Common markets | AO2 | |

# Learning objectives

<table>
<tr><th>4.4 Economic integration</th><th>Depth</th><th>Diagrams & calculations</th></tr>
<tr><td>Advantages and disadvantages of trading blocs;<br><br>Advantages, including:<br>• trade creation (HL only)<br>• greater access to markets offer potential for economies of scale<br>• with freedom of labour, there are greater employment opportunities<br>• membership in a trading bloc may allow for stronger bargaining power in multilateral negotiations<br>• greater political stability and cooperation<br><br>Disadvantages, including:<br>• trade diversion (HL only)<br>• loss of sovereignty<br>• challenge to multilateral trading negotiations</td><td>AO1</td><td></td></tr>
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# Learning objectives

| 4.4 Economic integration | Depth | Diagrams and calculations |
|---|---|---|
| Monetary union | AO2 | |
| **Advantages and disadvantages of monetary union (HL only)** | **AO3** | |
| The World Trade Organization (WTO)<br>• Objectives and functions<br>• Factors affecting the influence of the WTO, including:<br>    • difficulties of reaching agreement on services/primary products<br>    • unequal bargaining power of members | AO2 | |

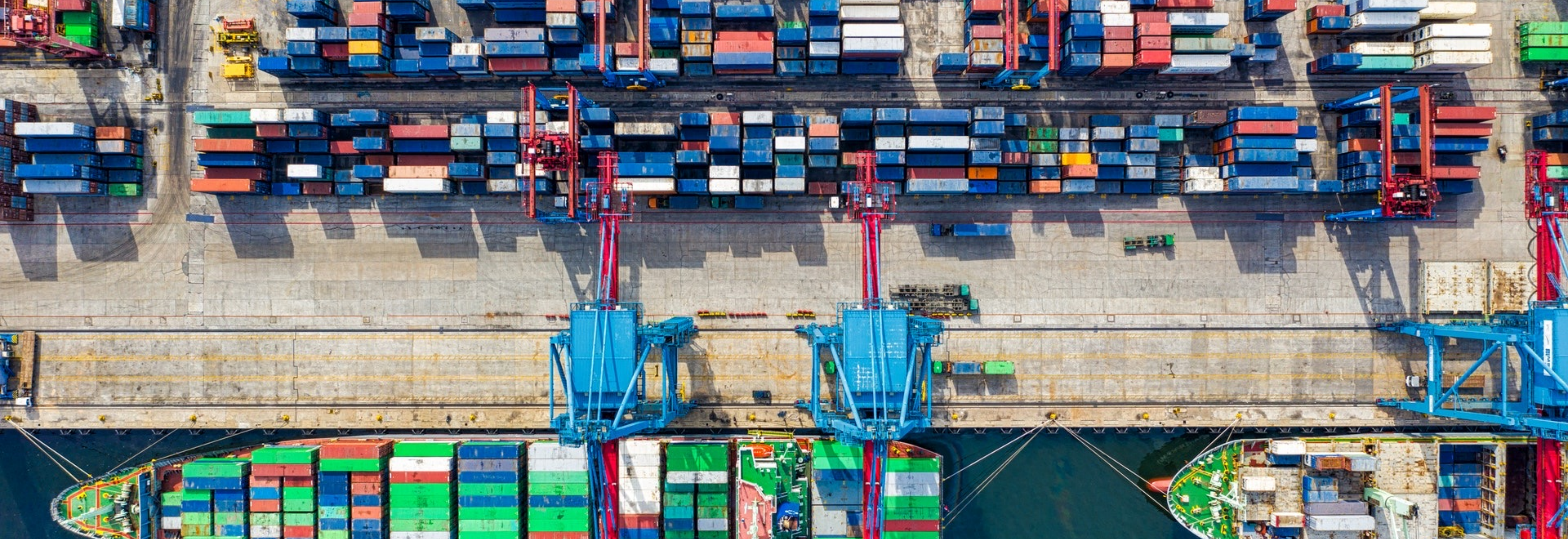
# Introduction

**Economic integration** refers to the process of countries becoming more interdependent and economically unified. There are three main types of economic integration:

**Preferential Trade Agreements (PTAs)**

**Trading Blocs**

**Monetary Unions**



# Real world example

**Article:** UK starts talks to join Asia-Pacific free trade pact

What are the costs and benefits towards the UK of joining the Comprehensive and Progressive Agreement for Trans-Pacific Partnership (CPTPP)?

# Preferential Trade Agreements (PTAs)

**A preferential trade agreement (PTA)** is an agreement between two or more countries to lower trade barriers between each other. Member states or governments sign a trade deal consenting to special or favorable terms and conditions of trade.

# Types of Preferential Trade Agreements

- A bilateral trade agreement - an agreement between two countries.
- A multilateral trade agreement - involves an agreement between three or more countries.

# Examples of PTAs – CEPA

The **Closer Economic Partnership Arrangement** (**CEPA**) is a PTA between Hong Kong and China. It aims to strengthen trade and investment cooperation by:

- Progressively reducing or eliminating barriers to trade
- Reducing substantial discriminatory measures
- Promoting trade and investment

# Examples of PTAs – ASEAN

The **Association of Southeast Asian Nations (ASEAN)** is a PTA comprising of 10 Asian countries.

It aims to achieve cooperative peace and shared prosperity by:

- Accelerating economic growth, social progress and cultural development in the region
- Promoting regional peace and stability by adhering to the principles of the United Nations Charter.

# Trading Blocs

A **trading bloc** is a group of countries that have agreed to reduce trade barriers for the purpose of encouraging free or freer trade and cooperation. The 3 main types of trading blocs include free trade areas, customs unions, and common markets.

# Free Trade Areas

**Free trade areas (FTAs)** are the most common type of trading bloc, where a group of countries agree to remove trade barriers between themselves.

Members can decide the level of trade barriers towards non-member countries.

# Examples of FTAs – USMCA

The **United States–Mexico–Canada Agreement** (**USMCA**) is the successor of NAFTA, and aims to:

- Eliminate barriers to trade
- Promote conditions of fair competition
- Increase investment opportunities
- Protect intellectual property rights
- Establish procedures for resolving disputes
- Further trilateral, regional and multilateral cooperation.


# Real world example

The [Regional Comprehensive Economic Partnership (RCEP)] is an FTA consisting of 13 east Asian countries.


# Customs Unions

A **customs union** is similar to FTAs, except members must adopt a common external trade policy towards all non-member countries.

# Examples of Customs Unions – CEFTA

The CEFTA (Central European Free Trade Agreement) comprises of seven countries. It aims to:

- Expand international trade in goods and services
- Promote FDI using fair regulations
- Eliminate the Technical Barriers to Trade
- Protect intellectual property rights
- Facilitate negotiations on regional trade policy.

# Examples of Customs Unions – SACU

The SACU (South African Customs Union) comprises of five countries and aims to maintain the free trade of goods between member countries.

It provides for a common external tariff and a common excise tariff, and revenues are shared among members systematically.


# Common Markets

In **common markets,** member countries impose common external trade policies and aims to eliminates **all** trade barriers between them. Factors of production i.e. land, labor, capital, and enterprise can flow freely between member states.

# Examples of Common Markets – Schengen Area

The **Schengen Area** is a common market consisting of 26 European countries, of which 22 are EU countries.

It aims to allow for free movement of labor between countries within the Schengen area without being checked or having to show their passports.

# Over to you…

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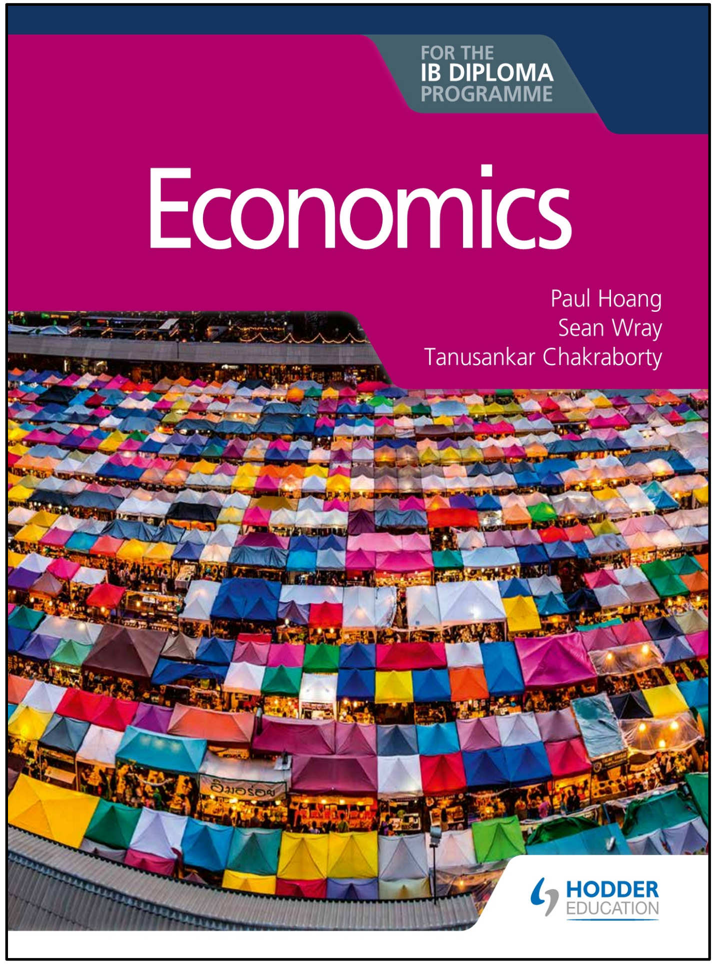
- [10 marks]




# Trade Creation (HL only)

**Trade creation** occurs when demand shifts from higher-cost producers to lower-cost producers within a trading bloc as a result of its formation.

# Trade Diversion (HL only)

**Trade diversion** occurs when demand shifts from lower-cost producers outside a trading bloc to higher-cost producers within the bloc as a result of its formation.

# Advantages of Trading Blocs

- Improved resource allocation, efficiency in production, and greater economic growth
- Increased competition allow for lower prices and greater consumer choice
- Producers can expand to larger markets, allowing them to achieve economies of scale
- With freedom of labor, there are greater employment opportunities
- Improved political relations and cooperation

# Disadvantages of Trading Blocs

- Inefficient producers will suffer
- Importing essential goods can reduce national sovereignty
- Increases discrimination for non-member countries
- Unequal distribution of gains and losses
- Reduces government tariff revenue.

# Monetary Union

A **monetary union** is formed when the member countries of a common market adopt a common currency and a common central bank responsible for monetary policy.

# Monetary Union

Member states do not have flexibility in exercising their own monetary policy.

Forming a monetary union requires potential members to limit inflation, government deficits, and government debt.

# Examples of Monetary Unions

The **European Union (EU)** is a monetary union comprising of 27 member states, sharing the common currency Euro (€).

The EU's monetary policy is implemented by the **European Central Bank (ECB)**.

Members follow the Maastricht treaty to promote sustainable economic convergence, avoid excessive government deficits, and limit government debt.

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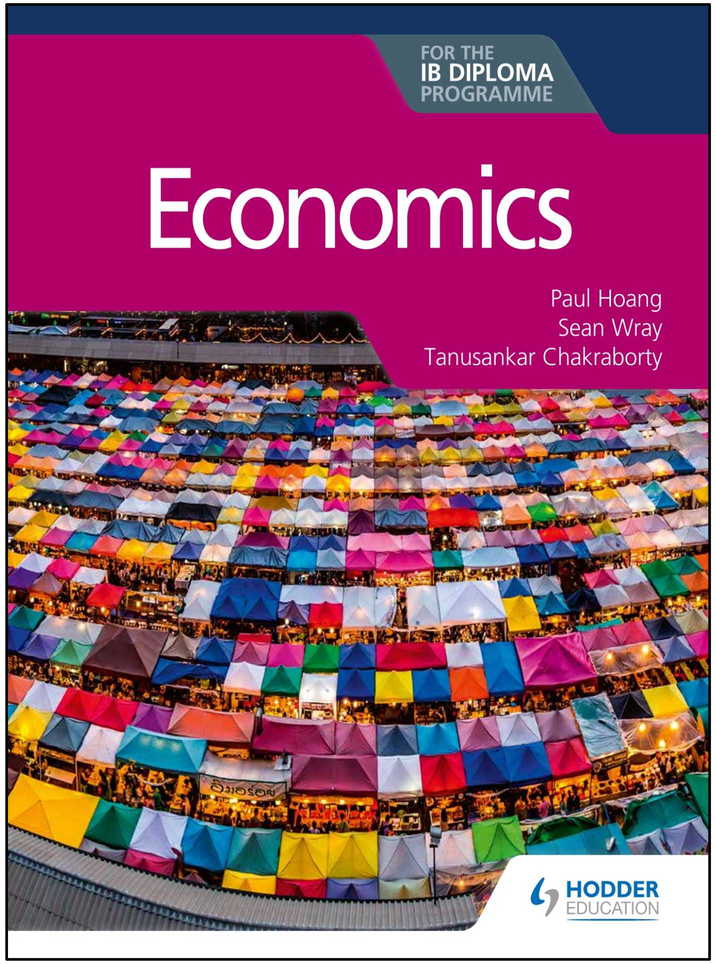
- [10 marks]



# Advantages of Monetary Union (HL only)

- A single currency eliminates exchange rate risk and uncertainty
- A single currency eliminates transaction costs.
- A single currency encourages price transparency.
- A single currency promotes a higher level of inward investment.
- Low rates of inflation give rise to low interest rates, more investment and increased output.

# Disadvantages of Monetary Union (HL only)

- A single currency involves loss of monetary policy as an instrument of economic policy.
- Monetary policy pursued by the single central bank impacts differently on each member
- Fiscal policy is constrained by the convergence requirements.
- A single currency involves loss of exchange rates as a mechanism for adjustment.
- Free movement of people may lead to overpopulation in certain areas.

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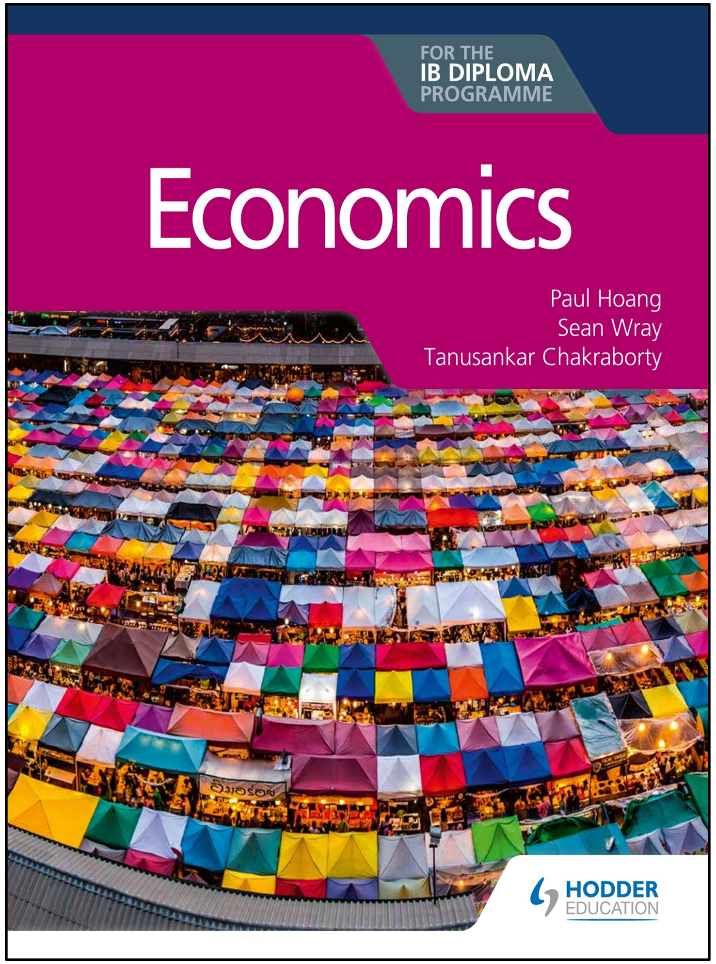
- Paper 1 Exam Practice Question 30.3
- [10 marks]



# The World Trade Organisation (WTO)

The **World Trade Organization (WTO)** was established in 1995 by 123 member countries to:

- Promote trade liberalization
- Oversee multilateral trade agreements
- Resolve trade disputes between member states

In some special circumstances, the WTO will support maintaining trade barriers:

- Environmental protection
- National security
- Protecting consumers from diseases (bird and swine flu from poultry and pork).

# The World Trade Organisation (WTO) – objectives

There are six interrelated objectives of the WTO as the core principles of an effective multilateral trading system:

1. Non-discrimination of member nations
2. More open international trade
3. Predictable and transparent trade policies
4. Promoting competition and preventing protectionism
5. Support for less economically developed countries
6. Protecting the environment.

# The World Trade Organisation (WTO) – functions

The WTO has five functions to ensure that trade between countries flows smoothly, predictably and freely.

1. Platform for trade negotiations including goods, services, and intellectual property
2. Implementation and monitoring of trade agreements
3. Forum for systematic trade disputes resolutions
4. Building trade capacity for developing countries
5. Outreach to promote economic co-operation and growth between countries.

# The World Trade Organisation (WTO) – limitations

Many argue that the WTO has had limited influence and success in certain areas of trade.

- High income countries continue to subsidize domestic production of primary goods, while imposing tariffs on primary good imports to protect domestic jobs.
- WTO is often in favor of large multinational companies and high-income countries.

Test your knowledge on this unit: Kahoot!