

# Module 6: Foreign Policy

## Topic 3 Content: Economic Organizations

### Introduction



**Demi Tracy:** The expansion of free and open trade is not only an important part of American economic policy, it is an important part of American foreign policy as well. Our foreign correspondent, Emily Airheart, and our financial analyst, Cain S. Hayek, are in the studio today to examine some different international economic organizations.

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#### Global Guide



**Emily Airheart:** Thank you, Demi. Welcome to this special economic edition of *Global Guide*. Free trade expands borders in order to sell goods and services, grow the economy, and raise the wages of citizens. It also gives countries access to products that would be unavailable otherwise. This could include simple goods, like fresh fruit for countries located in colder climates. It could also include essential resources, like lumber and oil, which a nation may lack. Cain, what should our audience understand about the importance of free trade?

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#### Economic Organizations



**Cain S. Hayek:** There is plenty for our audience to understand, but I will try my best to keep things simple. Before we can discuss the benefits of a free market economy and the organizations that promote this, we need to define a few terms first.

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#### Protectionism

## Protectionism

- Economic policy that shields a country's domestic industries from foreign competition
- Usually done through tariffs or restrictive quotas on imports
- **Tariffs:** taxes on imports or exports
- **Quotas:** limits on the number or value of goods and services that may be imported or exported
- The opposite of free trade, which is focused on eliminating trade barriers wherever possible



**Cain S. Hayek:** The first term we will discuss is protectionism. Protectionism is an economic policy that attempts to shield a country's domestic industries from foreign competition. This is usually done through tariffs or restrictive quotas on imports. Tariffs are taxes on imports or exports. Quotas are limits on the number or value of goods and services that may be imported or exported. Protectionism is considered the opposite of free trade, which is focused on eliminating trade barriers wherever possible.

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**Absolute Advantage**

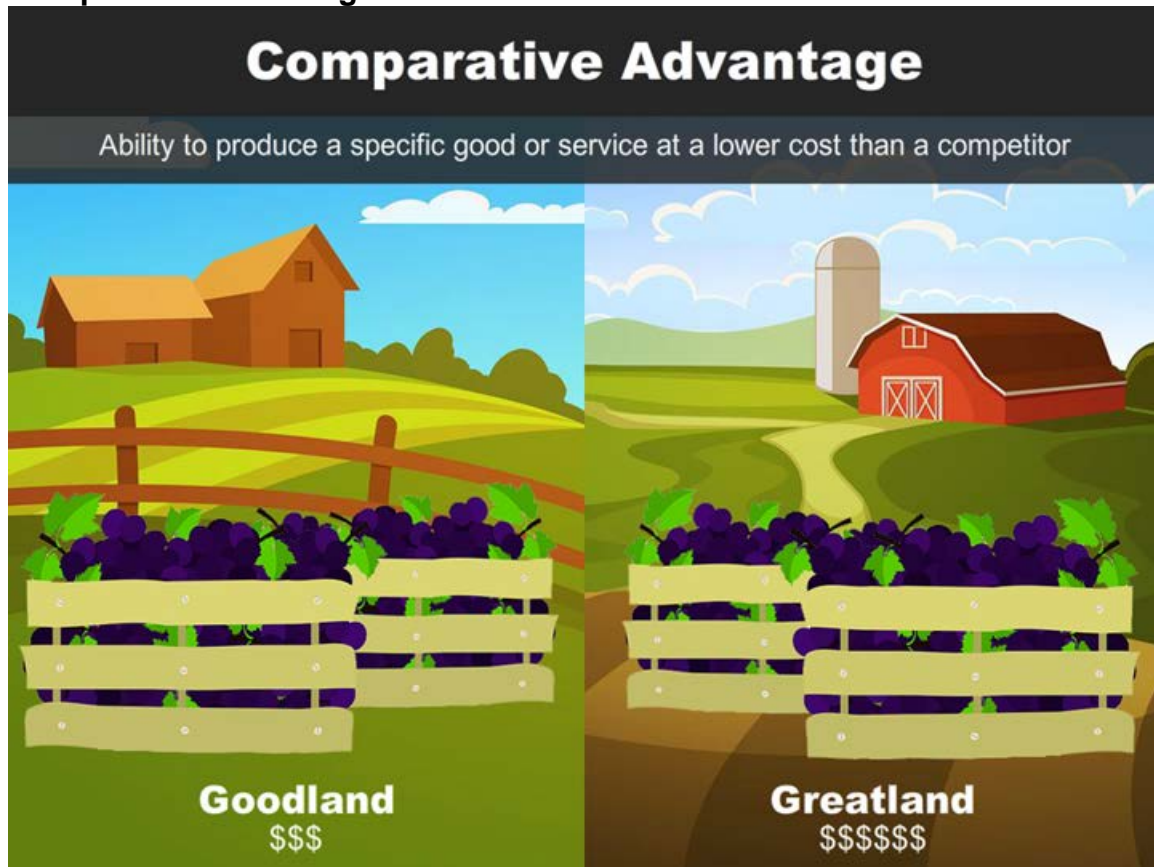


**Cain S. Hayek:** Our next term is absolute advantage. Absolute advantage is a nation's ability to produce more goods or services than competitors with similar resources. To help illustrate this concept, picture two hypothetical countries, Goodland and Greatland. Imagine that Goodland grows 25 million acres of tomatoes annually, and Greatland grows 50 million acres of tomatoes annually. You would say that Greatland has an absolute advantage over Goodland, since during the same period of time, Greatland is able to produce more tomatoes.



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**Comparative Advantage**



**Cain S. Hayek:** Sticking with our two imaginary countries, let's say that both Greatland and Goodland are able to produce 50 million acres of grapes a year; however, Goodland is able to produce its grapes at a much lower cost than Greatland. This is called a comparative advantage. A comparative advantage is defined as the ability to produce a specific good or service at a lower cost than a competitor, due to some type of advantage. Goodland's climate is better suited to grow grapes, and it has better technology to harvest them, meaning it is able to produce grapes at a relatively lower cost than Greatland. If Goodland exports its cheap grapes to Greatland and imports Greatland's extra tomatoes, both countries benefit. Comparative advantage is one of the main economic arguments for free trade. Nations are able to expand their output with the same amount of resources, increasing economic efficiency and financial gains. American foreign policy subscribes to this economic theory.

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**World Trade Organization**

# WORLD TRADE ORGANIZATION



## World Trade Organization

- America increases free trade through membership in organizations.
- WTO is an international group focused on promoting free trade on a global scale.
- It was started in 1995, and considers more than 150 nations as members.
- WTO provides a forum for members to negotiate, handles disputes between countries, and administers trade agreements.
- It attempts to protect the interests of countries with weaker economies by preventing predatory trade practices by nations with larger and stronger economies.

**Cain S. Hayek:** In order to help increase free trade, America is a member of some important international economic organizations. The World Trade Organization is one of these organizations. This organization, also known as the WTO, is an international group focused on promoting free trade on a global scale. The WTO was started in 1995, and it currently considers more than 150 nations as members. To help promote the unrestricted flow of goods and services, the WTO provides a forum for members to negotiate, handles disputes between countries, and administers trade agreements. The organization attempts to protect the interests of countries with weaker economies by preventing predatory trade practices by nations with larger and stronger economies. Even though the World Trade Organization works to remove barriers to free trade, it does allow some forms of protection.

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#### International Monetary Fund

## IMF and the World Bank



- The IMF was established in 1944 to help the global economy recover from World War II and prevent another great depression.
- Nearly every nation in the world is a member.
- Its headquarters are located in Washington, D.C.
- The IMF works to secure financial stability, increase international trade, and promote economic growth around the world.
- It offers short-term loans and technical assistance to developing nations, and also helps monitor the global economy.

Next

**Cain S. Hayek:** Another organization worth mentioning is the International Monetary Fund, or the IMF. The IMF was established in 1944 to help the global economy recover from World War II and prevent another great depression. Nearly every nation in the world is a member, but its headquarters are located in Washington, D.C. Rather than help rebuild post-World War II Europe, these days the IMF works to secure financial stability, increase international trade, and promote economic growth around the world. It offers short-term loans and technical assistance to developing nations, and also helps monitor the global economy.



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#### The World Bank

## IMF and the World Bank



**THE WORLD BANK**  
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- The World Bank was developed alongside the IMF and is also headquartered in Washington, D.C.
- It began by offering financial assistance for the reconstruction of post-World War II Europe.
- It offers loans to developing nations in Africa, Asia, and Latin America.
- These loans are used to develop a nation's infrastructure or grow a specific industry in a nation.
- The World Bank works closely with the IMF to formulate policies that will help stabilize the economy.

Next

**Cain S. Hayek:** The World Bank was developed alongside the International Monetary Fund and is also headquartered in Washington, D.C. It began by offering long-term loans and financial assistance for the reconstruction of post-World War II Europe, but it has grown to include developing nations in Africa, Asia, and Latin America. These loans are usually geared toward developing a nation's infrastructure, such as roads and utilities, or growing a specific industry in a nation, like agriculture. The World Bank works closely with the IMF to formulate policies that will help stabilize the economy.

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#### Free Trade Agreements

## Free Trade Agreement

- American foreign policy works for the liberalization of trade by signing free trade agreements with other nations.
- A free trade agreement is a signed agreement between at least two countries to reduce tariffs, quotas, or other barriers to free and open trade.
- The United States has free trade agreements in 20 different countries.
- The North American Free Trade Agreement was signed in 1994, and reduces government barriers to trade in the United States, Canada, and Mexico.



The image shows a map of North America with the United States, Canada, and Mexico highlighted in yellow. The acronym 'NAFTA' is printed in large, bold, black letters across the center of the highlighted region. The surrounding oceans and other landmasses are shown in light blue and grey.

**Cain S. Hayek:** American foreign policy also works for the liberalization of trade by signing free trade agreements with other nations. A free trade agreement is a signed agreement between at least two countries to reduce tariffs, quotas, or other barriers to free and open trade. As of 2015, the United States has free trade agreements in 20 different countries. The most well-known is probably NAFTA, or the North American Free Trade Agreement. This agreement was signed in 1994, and reduces government barriers to trade in the United States, Canada, and Mexico. The free trade zones created by these agreements help promote fair competition and increase investment opportunities for the countries involved.

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**Ending of Episode**



**Demi Tracy:** Thank you, Cain. Critics of free trade cite the risk of a trade deficit or the lowering of wages as reasons to support protectionism. Although these risks are real and should be managed, we cannot neglect international trade. It is inevitable in the modern world. In addition to the financial benefits that comparative advantage offers in a free market, when nations are involved in international trade, it creates economic ties that offer a degree of stability.