Why do Countries Trade?

Part I

AED/IS 4540
International Commerce and the World Economy

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A Single Market under Autarky

Market with no trade – autarky

Equilibrium at A, with price $P^A$, quantity $Q^A$

c is consumer surplus

h is producer surplus

g are variable costs

total benefit is $(c+h)$

- **P (price)**
- **Q (quantity)**
- **S (supply)**
- **D (demand)**

Market equilibrium at A with price $P^A$, quantity $Q^A$.
Excess Supply - Exports

World Market

Chinese Market

Excess Supply

Chinese Exports
Excess Demand - Imports
A Single Market with Trade

US Market

World Market

Chinese Market

Imports = Exports
Who Wins and Who Loses?

US Market

Consumer gain (a+b)
Producer loss (a)
Net benefit (b)

World Market

Gains from trade (b+g)

Chinese Market

Consumer loss (e+f)
Producer gain (e+f+g)
Net benefit (g)
Who Wins and Who Loses?

- In each country, there are net gains, i.e., consumer surplus \( b \) in US, and producer surplus \( g \) in China.

- Consequently, the world gains from trade, i.e., it is a positive-sum activity.

- However, gains from trade are not necessarily evenly distributed across countries, i.e., \( b > g \) in this particular example.

- Trade depends on there being a difference between autarky prices – why might they differ?

- Could be technology, or could be relative resource endowments.