

## THE IMPACT OF INTERNATIONAL TRADE AND COMPETITION MARKET ON DEVELOPING COUNTRIES

Jonida Lamaj  
Marin Barleti University, Albania  
jonidalamaj@gmail.com

### **Abstract:**

International trade plays a key role in a country economy and the global economy. As a rule, the foreign policies related to trade's barriers are the most difficult to achieve, but they play a significant role for the business sector and its competitors. Through this paper I will analyse three important issues related to the international trade and the competition market: the importance of free trade in an economy; the way a capitalist economy influences free trade and how small numbers of suppliers lead to imperfect competition. This article tries to answer important questions related to the main theme such as reasons as why is free trade important, with a special view on the European Union case; what does globalization brings to the trade economy; and is monopoly safe in the long run? Additional concepts about developing countries, various economic systems, will be part of this paper as well. The abstract of my paper has been presented and published at the Make Learn & TIIM 2015 International Conference. Today, most markets are populated and often manipulated by large companies. Some of them are the only supplier (monopoly) or, more typically, one of the few suppliers (oligopoly) – not just at the national level but increasingly at the global level. The advancement of capitalism in the Western Europe countries and their offshoots in the nineteenth century is often attributed to the spread of free trade and free market. It is only because the government in these countries, it is argued, did not tax or restrict international trade and more generally did not interfere in the work of the market that these countries could develop capitalism. No monopoly is safe in the long run. Companies that once had near monopoly of their respective markets and had been considered invincible have lost such positions and even disappeared into the dustbin of history.

*Keywords: international trade, competition market, capitalist economy, open borders, monopoly*

## 1. INTRODUCTION

International trade (free trade) can bring many benefits. By providing a bigger market, it allows producers to produce more cheaply, as producing a larger quantity usually lowers the costs. This aspect is especially important for smaller economies, as they will have to produce everything expensively, if they cannot trade and have a bigger market. By increasing competition, international trade can force producers to become more efficient, insofar as they are not developing country firms that would get wiped out by vastly superior foreign firms. It might also produce innovation by exposing producers to new ideas. International trade is particularly important for developing countries. In order to increase their productive capabilities and thus develop their economies, they need acquire better technologies. For these countries it would be unthinkable not taking advantage of all the technologies they can import, whether in the form of machines or technology licensing or technical consultancy. However great an economic theory may be, it is specific to its time and space. To apply it fruitfully, therefore, it is required a good knowledge of the technological and institutional forces that characterize the particular markets, industries and countries that we are trying to analyze with the help of the theory.

## 2. WHY IS FREE TRADE IMPORTANT?

Free trade improves people's lives. It enables each person to specialize in doing what they do best. It also encourages competition in the supply of goods and services, which in turn incentivizes people to develop better, less expensive goods and services. Over time, these improvements result in increases in output and productivity. The Index of Economic Freedom estimates that "trade openness" (the degree to which economies are open to trade in goods, services, capital and people) is a significant determinant of GDP. For over 50 years, Hong Kong and Singapore have essentially been free-trade zones, which explain in large part why, during that time, they have grown from small fishing ports into enormously wealthy cities.

Policy-makers around the world learned from these examples and recognized how important the freedom of trade is in order to improve welfare and increase standards of living. As a result, trade barriers have been falling globally since the end of the Second World War. According to the World Trade Organization, the average "applied" tariff in developed countries has fallen from over 10 per cent in 1980 to under 5 per cent today. The average tariff applied in developing countries has fallen, too, from over 30 per cent in the early 1980s to under 15 per cent in 2000. Partly as a result of these falling barriers, trade flows have increased exponentially. The reduction and removal of trade barriers, particularly in some of the world's currently fastest growing economies, has enabled more than 500 million people to lift themselves out of poverty in the past 30 years, including 400 million in China and tens of millions in India, Chile, New Zealand, etc.

### **2.1. Based on the different economic theories, Free Trade will provide a number of important benefits**

#### *The theory of comparative advantage/specialization*

According to such theory, if a country does specialize in goods where this country have a lower opportunity cost, it should be translated to an increase in economic welfare for all countries. Free trade enables countries to specialize in those goods where they have a comparative advantage.

#### *Free trade will increase exports*

As well as benefits for consumers importing goods, the goods exporting firms in a country that has a comparative advantage will also see a big improvement in economic welfare. Lower tariffs on a country exports will enable a higher quantity of exports boosting that country jobs and economic growth.

#### *Free trade and its implications to the Economies of Scale*

If a country can specialize in certain goods it can benefit from economies of scale and lower average costs. This reasoning is especially true in industries with high fixed costs or industries that require high

levels of investment. The benefits of economies of scale will ultimately lead to lower prices for consumers.

#### *Free trade will increase competition*

Because with the increasing of trade domestic firms will face more competition from abroad, there will be more incentives to cut costs and increase efficiency. It may prevent domestic monopolies from charging too high prices.

#### *Trade is an engine of growth*

World trade has increased by an average of 7% since the 1945, causing this to be one of the big contributors to economic growth.

#### *Make use of surplus raw materials*

Countries in the Middle East such as Qatar are very rich in reserves of oil but without trade there would be not much benefit in having so much oil. Japan on the other hand has very few raw material without trade it would be very poor.

#### *Tariffs may encourage inefficiency*

If an economy protects its domestic industry by increasing tariffs industries may not have any incentives to cut costs.

## **2.2. Globalizations and expansion of international trade**

Globalization refers to the worldwide phenomenon of increased technological, economic, and cultural interconnectedness between nations. In a globalized economy, economic activity is unrestricted by time zones or national boundaries. It is essentially capitalism on a global, rather than a national, scale.

Nowdays, products are rarely made in one place from start to finish. Instead, they are assembled over a long series of individual steps often located in different parts of the world.

This trend has accelerated dramatically since the 1980s, as technological advances have made it easier for people to travel, communicate, and do business internationally.

The expansion of international trade and foreign investment was sparked not only by technological progress, but also by two major sociopolitical developments of the 1980s. One of these was the collapse of global communism. The fall of the Berlin Wall and the subsequent dissolution of the Soviet empire freed some 400 million people from the shackles of closed centrally commanded economic systems. The second development was the demise of the Third World's reliance upon import substitution, a trade and economic policy founded on the idea that a developing country can increase its wealth by importing as few goods as possible and relying instead on locally produced substitutes. When import substitution proved to be a colossal failure, struggling countries all over the world, starting with Chile in the mid-1970s and China later that decade began opening their markets and welcoming foreign investment.

The growth of new economic powerhouses in the end of the 20th century, such as China, India and Brazil, has intensified competition in terms of the price and quality of goods being produced, and, perhaps more importantly, for access to energy and raw materials. At the same time, these countries are creating a new group of affluent consumers and their economies are more open than they were 10 to 15 years ago. For instance, Chinese import tariffs fell from 19.8 % in 1996 to 4.7 % in 2012. Over the same period, the decrease in India was 20.1 % to 7 % and in Brazil 13.8 % to 10 %, although other, less visible, barriers to exports still remain. Open borders have allowed companies to source the cheapest things from across the globe and offer the best deals to consumers. In addition open borders have increased competition among producers, forcing them to cut their costs and improve their technologies. Even from a the consumers perspectives, benefits from ever increasing trade include lower prices and greater choice power, as imported food, consumer goods and components for manufactured products become cheaper.

Opponents of globalization characterize the phenomenon as a form of Western expansionism and cultural imperialism, claiming that it will merely increase the opportunities for wealthier nations to take advantage of poorer ones. This happens, the critics say, because multinational corporations can exploit the cheap labor and lax regulations typical of developing countries where there are no labor unions. Believing, despite overwhelming evidence to the contrary, that a planned economy ensures the greatest economic benefit to the poor, the anti-globalization movement tends to favor socialism over capitalism. It also warns that globalization could eradicate regional diversity and lead to a homogenized world culture where “native” cultures are swallowed up by Western traditions.

Supporters of globalization respond by pointing out that since the 1980s, every nation that has experienced an increase in its manufacturing output has also seen its per capita income rise, that nations open to trade tend to be much more prosperous than nations with closed economies, and that the increased wages spawned by globalization correlate with reduced poverty and improved living conditions for all. The most impressive gains in this regard have been realized in East Asia.

The two most prominent pro-globalization entities today are the World Trade Organization and the World Economic Forum. The former, consisting of 144 members, was created to establish a set of rules to govern global trade through the process of member consensus. The latter is a private foundation that does not possess decision-making power but is a powerful networking forum for many of the world’s business, government, and not-profit leaders.

### **2.3. European Union and free trade**

The European Union has positioned free trade at the core level of the community economic policy. The Union’s trade policy is an integral ingredient of its wider 2020 strategy to boost employment and create a more modern, viable and sustainable economy. A vibrant domestic economy requires the Union to be increasingly competitive abroad. While free trade has been widely accounted as very important for economic growth and job creation, in the union’s case this need is even more pressing. Because two thirds of imports in EU are raw materials, intermediary goods and components needed by EU manufacturers, it is necessary that Europe’s market remains open to such supplies. Restricting their flow or raising the cost of imports would backfire by increasing the costs and reducing the competitiveness of European companies both at home and abroad. That is why free trade is viewed to be the tool that can help pull the EU out of the present crisis. The crises which began in the United States with the sub-prime meltdown in 2007–08 exposed the inherent weaknesses within the EU. Along with the deepening of the single market and targeted Europe-wide investment in areas such as research, education and energy, free trade is one of the key triggers to stimulate the European economy.

Open markets generate more economic growth and more and better jobs for Europe and its partners. In EU’s case data are overwhelming. In 2011, 14 % of the EU workforce depended directly or indirectly on exports to the rest of the world. This has increased by around 50 % since 1995. Add to that the growing importance of foreign direct investment for job creation, with American and Japanese companies now employing over 4.6 million people in Europe. Trade liberalisation creates additional opportunities for innovation and stronger productivity growth. Trade and investment flows spread new ideas and innovation, new technologies and the best research, leading to improvements in the products and services that people and companies use. The EU countries experience has showed that a 1 % increase in the openness of the economy results in a 0.6 % rise in labour productivity the following year.

### **2.4. European Union and developing countries**

A developing country, also called a less-developed country, is a nation with a lower standard of living, underdeveloped industrial base, and low Human Development Index (HDI) relative to other countries. On the other hand, since the late 1990s developing countries tended to demonstrate higher growth rates than the developed ones. There is no universal, agreed-upon criterion for what makes a country developing versus developed and which countries fit these two categories, although there is general reference points such as a nation’s GDP per capita compared to other nations.

The designations “developed” and “developing” are intended for statistical convenience and do not necessarily express a judgment about the stage reached by a particular country or area in the

development process. The UN also notes that Japan in Asia, Canada and the United States in northern America, Australia and New Zealand in Oceania, and Western Europe are considered "developed" regions or areas. In international trade statistics, the Southern African Customs Union is also treated as a developed region and Israel as a developed country; countries emerging from the former Yugoslavia are treated as developing countries.

On the other hand, according to the classification from International Monetary Fund (IMF) before April 2004, all countries of Central and Eastern Europe as well as the former Soviet Union (USSR) countries in Central Asia (Kazakhstan, Uzbekistan, Kyrgyzstan, Tajikistan and Turkmenistan) and Mongolia, were not included under either developed or developing regions, but rather were referred to as "countries in transition"; however they are now widely regarded (in the international reports) as "developing countries". Developing countries are, in general, countries that have not achieved a significant degree of industrialization relative to their populations, and have, in most cases, a medium to low standard of living. There is a strong association between low income and high population growth.

The Union actively encourages developing countries to use trade to build up their own economies and improve living standards. Growth in trade can enhance their export earnings and promote diversification of their economies away from commodities and raw materials. To help developing countries export, the Union was the first organisation in the world to grant a generalised system of preferences (GSP), in 1971, under which it introduced preferential import rates to all developing countries, giving them vital access to European markets. However, over the past four decades global economic and trade balances have shifted tremendously. Several more advanced developing countries have successfully integrated into the world trading system, while a greater number of poorer countries have been increasingly lagging behind. In the current competitive environment, tariff preferences must go to those countries most in need. As a result, the reformed Generalised Scheme of Preferences (GSP) — effective from 2014 — focuses the benefits on the least developed countries (LDCs) and other low and low-middle income economies without other preferential access to the EU. There are currently 88 such countries (Page 13 EU trade: <http://ec.europa.eu/trade>).

### **3. HOW THE CAPITALIST ECONOMY INFLUENCES FREE TRADE**

Capitalist economy is an economy in which production is organized in pursuit of profit, rather than for own consumption or for political obligation. Capitalism, also is known as the free-enterprise or free-market system, is the economic structure that permits people to use their private property however they see fit, with minimal interference from the government. Under capitalism, people are free to work at jobs of their own choosing, to try to sell their products or services at whatever prices they wish, and to select from among various product and service providers for the best value.

Markets have changed. In Smith's time, markets were largely local or at most national in scope, except in key commodities that were traded internationally or a limited range of manufactured goods. These markets were served by numerous small-scale firms, resulting in the state that economists these days call perfect competition, in which no single seller can influence the price. Today, most markets are populated and often manipulated by large companies. Some of them are the only supplier (monopoly) or, more typically, one of the few suppliers (oligopoly) – not just at the national level but increasingly at the global level. Unlike the small companies in Adam Smith's world, monopolistic or oligopolistic firms can influence market outcomes – they have what economists call market power. A monopolistic firm may deliberately restrict its output to raise its prices to the point that its profit is maximized. Oligopolistic firms cannot manipulate their markets as much as a monopolistic firm can, but they may deliberately collude to maximize their profits by not under-cutting each other's prices – this is known as a cartel. As a result, most countries now have a competition law in order to counter such anti-competitive behaviours breaking up monopolies and banning collusion among oligopolistic firms. Monopolistic and oligopolistic firms were considered to be theoretical curiosities even a few decades ago. Today, some of them are even more important than monopolistic and oligopolistic firms in shaping our economy. Exercising their powers as one of the few buyers of certain products, sometimes on a global scale, companies like Wal-Mart, Amazon, Tesco and Carrefour exercise great, sometimes even defining influence on what gets produced where, who gets how big a slice of profit and what consumers buy. The advancement of capitalism in the Western Europe countries and their offshoots in the nineteenth century is often attributed to the spread of free trade and free market. It is only because the government in these countries, it is argued, did not tax or restrict international trade

and more generally did not interfere in the working of the market that these countries could develop capitalism. Capitalism has undergone enormous changes in the last two and a half centuries. Today competition is among huge multinational companies with the ability not only to influence prices but to redefine technologies in a short span of time and to manipulate consumer tastes through brand image building and advertising.

Capitalism creates wealth through advancing continuously to ever higher levels of productivity and technological sophistication. For this process to succeed it requires that the "old" be destroyed before the "new" can take over. Technological progress, the ultimate driving force of capitalism, requires the continuous discarding of obsolete factories, economic sectors, and even human skills. The system rewards the adaptable and the efficient, while it punishes the redundant and the less productive. Although capitalism eventually distributes wealth more equally than any other known economic system, as it does tend to reward the most efficient and productive, it tends to concentrate wealth, power, and economic activities. Threatened individuals, groups, or nations constitute an ever-present force that could overthrow or at least significantly disrupt the capitalist system.

It should be noted that "pure" capitalism, unencumbered in any way by government, doesn't exist neither in the United States nor anywhere else in the world. Moreover, the capitalist system of present-day America differs in significant ways from other capitalist systems around the globe, just as it differs from the capitalism that existed in the U.S. at the turn of the 20th century. While private-property rights and certain amounts of economic freedom have always been part of American life since that time, those rights and freedoms have become increasingly weighted down by heavy governmental regulation.

Critics of capitalism believe it is imprudent to allow an unregulated market to run its course, and to permit private citizens to make their own economic decisions based on self-interest. Asserting that such systems are inherently chaotic and inefficient, these critics propose that government regulators and bureaucrats "experts" presumably unencumbered by the greed or the impulse for self-interest that motivates private citizens should be empowered to "manage" economies authoritatively. In response to these positions, the Ludwig von Mises Institute scholar Robert P. Murphy writes that "This view is flawed in two major respects. First it is impossible for a central authority to plan an economy. New technologies (if entrepreneurs have freedom to create new technologies), changes in consumer taste (if consumers have freedom to pursue their tastes), and innumerable variables that can affect production, distribution, and consumption of everything from newspapers to lawnmowers on national or international scale are simply not 'manageable' in the way socialist planners like to think they are. Second, the planning bias completely misunderstands the role of profit and loss in a market economy. Far from being arbitrary, a company's 'bottom line' indicates whether an entrepreneur is doing what makes sense if his product is one that people want and if he is using his resources in the best possible way."

The rise of modern capitalism changed all this. The fortunes of the big businessmen who emerged under capitalism are no longer depended upon the patronage of a few wealthy clients. Rather, these entrepreneurs began catering to the needs and desires of a newly empowered working class consisting of millions of people. By meeting those needs and desires, businessmen greatly increased their own wealth and influence. In the first days of the Industrial Revolution, workers were abused. Yet they organized into unions that protected their interests and changed capitalism itself, pressuring it to evolve from its early exploitative model to a more humane one. As a result, capitalism helped improve the lives of people in every social stratum. For example, the transition into the capitalist era brought a dramatic decrease in infant-mortality rates and a significant rise in life expectancy. Moreover, the average blue-collar worker under capitalism was far wealthier than the "bosses" of socialist economies.

#### **4. HOW SMALL NUMBERS OF SUPPLIERS LEAD TO IMPERFECT COMPETITION? IS MONOPOLY SAFE IN THE LONG RUN?**

Many economists talk of market failure when there is monopoly or oligopoly. In a market with a lot of competitors, producers do not have the freedom to set the price, as a rival can always undercut them until the point where lowering the price further will result in a loss. But a monopolistic or oligopolistic firm has the market power to decide, fully in the case of the former and partly in the case of the later, the price it charges by varying the quantity it produces. In the case of oligopoly, the firms can form

cartels and behave as if they are a monopoly, which allows them to charge the higher, monopoly, price. If a market is dominated by firms with market power, it is argued, the government may try to reduce the deadweight loss by reducing their market power. The case of natural monopoly, which is found in industries like electricity, water, gas and rail-ways pose a unique challenge. In these industries, having multiple suppliers each with their own networks of, say, water pipes or railways, increases the production cost as much that monopoly is the most cost efficient arrangement.

No monopoly is safe in the long run. Companies that once had near monopoly of their respective markets and had been considered invincible have lost such positions and even disappeared into the dustbin of history.

The global competitiveness report defines competitiveness as the set of institutions, policies, and factors that determine the level of productivity of a country. The level of productivity, in turn, sets the level of prosperity that can be reached by an economy. The productivity level also determines the rates of return obtained by investments in an economy, which in turn are the fundamental drivers of its growth rates. In other words, a more competitive economy is one that is likely to grow faster over time. Although the productivity of a country determines its ability to sustain a high level of income, it is also one of the central determinants of its return on investment, which is one of the key factors explaining an economy's growth potential. Many determinants drive productivity and competitiveness. Understanding the factors behind this process has occupied the minds of economists for hundreds of years, engendering theories ranging from Adam Smith's focus on specialization and the division of labour to neoclassical economists' emphasis on investment in physical capital and infrastructure, and, more recently, to interest in other mechanisms such as education and training, technological progress, macroeconomic stability, good governance, firm sophistication, and market efficiency, among others. While all of these factors are likely to be important for competitiveness and growth, they are not mutually exclusive, two or more of them can be significant at the same time, and in fact that is what has been shown in the economic literature.

The components that measure the competitiveness of a country are grouped into 12 pillars, such as: institutions, infrastructure, macroeconomic environment, health and primary education, higher education and training, goods market efficiency, labour market efficiency, financial market development, technological readiness, market size, business sophistication and innovation.

## **5. CONCLUSIONS**

Free trade can be beneficial to any country despite their stage of economic development, as it boosts the chance for economy efficiency, innovation, specialization, knowhow and technological capabilities acquisition. As we saw in the European Union's case, free trade is not only been correlated to economic growth and job creation in the community area, but as a tool to support the economic progress of developing countries.

Despite capitalism being the better known economic system for fairer distribution of wealth and in rewarding the most efficient and productive economic actors, it tends to concentrate wealth, power, and economic activities. For this reason the system is and will continue to be subject of debate and controversy from its followers and critics.

Competitiveness is viewed as the set of institutions, policies, and factors that determine the level of productivity of a country as well as its ability to sustain a high level of income. The competitive level of an economy determines the likelihood of its growth pace over time.

In nowadays global settings, the markets are populated and often manipulated by large companies, which have market power. To counter and mitigate the possibilities of anti-competitive behaviours, most countries now have a competition laws for breaking up monopolies and banning collusion among oligopolistic firms. Nevertheless, history has shown that no monopoly is safe in the long run. Companies that once had near monopoly of their respective markets and had been considered invincible have lost such positions and even disappeared into the dustbin of history.

## REFERENCE LIST

1. Autoriteti i Konkurrencës. 2006. *Politika Kombëtare e Konkurrencës*, Tiranë: Afërdita
2. Chang, H. (2014). *Economics: the user's guide*. USA: Pelican.
3. Edwards, S. (1992, July). Trade Orientation, Distortions and Growth In Developing Countries. (pp. 1- 37). *Journal of Development Economics*. Retrieved from <https://books.google.al/>
4. European Commission. (2014). *Free trade is a source of economic growth*. European Union: Luxemburg Publications Office of the European.
5. Gilpin, R. (2000). *The challenge of the global capitalism, the world economy in the 21<sup>st</sup> century*. New Jersey: Princeton University Press.
6. Guillén, M. (2003). *Multinationals, Ideology, and Organized Labor. The Limits of Convergence*. Princeton University Press.
7. Harrison, A. (1996). Openness and Growth: A Time-series, Cross-country Analysis for Developing Countries. *Journal of Development Economics*. Retrieved from <http://economicdiscussion.com/>
8. International Monetary Fund. (1998, May). *Advanced Economies List*. World Economic Outlook, (PDF).
9. International Monetary Fund. (2009, April). *Advanced Economies List*. World Economic Outlook, (PDF).
10. Lindblom, Ch. (2001). *The market system*. New Haven & London: Yale University Press.
11. Luttwak, E. (2000). *Turbo – Capitalism: Winners and Losers in the Global Economy*. New York: Haper Perennial.
12. Mankiw, G. (2007). *Principles of Economics* (4th ed.). Cengage Learning
13. Murphy, R. (2007). *The Politically Incorrect Guide to Capitalism*. Washington, DC: Regnery Publishing.
14. Papadopoulos, A. (2010). *The International Dimension of EU Competition Law and Policy*. Cambridge University Press.
15. Papajorgji, E. 2013. *E drejta ndërkombëtare dhe shqiptare e konkurrencës*, Tiranë: ILAR
16. Smith, A. (2005). *An inquiry into the nature & causes of the wealth of nations*. USA: an E-publishing, Pennsylvania State University.
17. Sullivan, A. & Sheffrin, S. (2003). *Economics: Principles in Action*. Upper Saddle River, New Jersey: Pearson Prentice Hall.
18. Suresh, R. (2010). *Economy & Society Evolution of Capitalism*. (pp.77-97) India: Sage publications.
19. World Economic Forum. (2015). *The global competitiveness report 2014-2015*, Geneva: Schwab, K.
20. Zajmi, I. (2006). *E Drejta Europiane*, Tiranë: EKD