

It of the efficiency  
argument. the theory



**ASSIGN  
BUSTER**

It only presents itself as an additional source of increased output and thus strengthens the case for international specialisation and free trade. 2. Gains from Trade: Gains of trade to the trading countries depend upon several factors including the volume of trade and the difference between domestic cost of production and international prices. It follows that, other things being equal, gains to the trading countries would increase under free trade. This is because free trade provides maximum opportunity for international specialisation and reduction in production costs. 3. Incentives: Free trade, by opening up markets and increasing demand, provides an incentive for producers to go in for improved techniques of production. This causes an all-round decline in production costs and addition to output.

To the extent trade is restricted, these incentives are also curbed. 4. Technology: Free trade allows easier flow of technical know-how. This also helps free-trading countries in accelerating their rate of economic growth. 5. Optimum Allocation of Resources: This is another dimension of the efficiency argument.

The theory of free trade assumes that in each free-trading country, demand pattern in the market represents true needs and aspirations of the society. Given this and other assumptions (like the flexibility of the trading economies), allocation of resources, in all the trading countries put together, has a basic tendency to conform to the needs and aspirations of their societies taken as a whole.

**Elaboration:**

The claim of optimum allocation of resources is a serious one and needs to be examined for assessing its validity, particularly because the case for free trade becomes very weak if income distribution is questionable and sub-optimal. In this connection, our reasoning is as follows: (i) The production pattern in free competitive economies follows the demand pattern expressed in the market. This is because producers produce goods with the aim of maximising their profit incomes (at least in the long run). Since goods with stronger demand tend to be more profitable to produce, it follows that the investment and production patterns of the economy also tend to be in conformity with the demand pattern expressed in the market. The productive resources are also allocated accordingly. (ii) However, what is questionable is the claim that the demand pattern in the market represents true needs and aspirations of the society.

It is noteworthy that demand pattern depends upon the incomes and preferences of the buyers. It follows that the demand pattern would reflect true needs and aspirations of the society only if the distribution of national income between members of the society is in accordance with their relative needs. This however, is not the case in a market economy. Let us see why. In a market economy, factors of production are in private ownership and incomes of individuals and households depend upon their ownership of factors of production and the rates at which they are paid for in the market.

However, the ownership of factors of production is not based upon relative needs of the members of the society. Also, an individual (or a household) can own several productive resources and in different quantities. More  
<https://assignbuster.com/it-of-the-efficiency-argument-the-theory/>

particularly, non-wage earners have higher incomes than wage earners. They have higher capacity to save and can further add to their non-wage sources of income. Thus, the net result is two-fold: (a) distribution of income is not on the basis of relative needs of the members of society, and (b) inequalities of income and wealth keep increasing with the passage of time.

6.

Preventing Monopolies: Free trade, like free markets, prevents monopolies with all the attendant benefits. If we agree with the traditional wisdom that competitive markets are superior to monopolistic ones, then this is a major advantage of free trade. However, these days, critics claim that free markets are not able to prevent the emergence of monopolies.

7. Vested Interests: Free trade helps in preventing the emergence of vested interests. As such it provides a better scope for the authorities to formulate and implement welfare-oriented measures. (The reader should recall the earlier argument that the effects of welfare-oriented measures would be felt in the external sector of the economy as well).

8. Living Standards: As human beings; we are always eager to improve our living standards. International trade feeds this urge through the demonstration effect. In addition, free trade has the advantage that it also provides better opportunities to satisfy this urge.