

The Economic Gains from Freer Trade



Introduction

Since the end of World War II, industrial economies have become increasingly reliant on foreign trade. The countries that comprise the Organization for Economic Cooperation and Development (OECD) traded more than U.S.\$5 trillion worth of goods and services in 1986. This was almost 40 per cent of their total production of goods and services. Canada alone traded over U.S.\$165 billion worth of goods and almost U.S.\$30 billion worth of services (excluding interest and other investment income) in 1986, the equivalent of 53 per cent of our total production.

Exports of goods and services have grown at a much faster pace than the value of total production in all industrial countries in the postwar period. But how does trade liberalization, and the resulting growth in international trade, lead to higher real output and a higher standard of living? What are the sources of the gains from international trade? These questions are addressed in this chapter.

Trade and Economic Performance

Past experiences abroad, and in Canada, demonstrate that trade liberalization has favourable consequences for economic growth.

(a) *Trade Liberalization Experiences Abroad*

In *Structural Adjustment and Economic Performance*, a report⁽¹⁾ to be published shortly, the OECD addresses the question of why the Western economies enjoyed such

an unprecedented boom during the 20 years following World War II, in sharp contrast to the stagnation of the prewar period. The single most significant factor identified in the OECD report is the unprecedented drive towards trade liberalization. The report notes:

“The liberalization of world trade on a multilateral basis was one of the outstanding successes of international economic co-operation in the first 20 years of the postwar period. The process of liberalization has still a long way to go, indeed it has in some significant respects been reversed in more recent years; but the experience of the past few decades makes it clear that greatly widened opportunities for trade, once durably established, have substantial positive effects on economic performance.”⁽²⁾

The report adds:

“It is a striking feature of postwar growth (and one which sets it apart from the inter-war years) that small countries – which rely most heavily on international trade – generally grew more rapidly than their larger counterparts. Moreover, their growth depended heavily on products characterized by economies of scale in production – products in which they could hardly have been efficient without access to foreign markets.”⁽³⁾

⁽¹⁾ Organization for Economic Cooperation and Development, Paris, 1988.

⁽²⁾ Op. cit.

⁽³⁾ *ibid.*