UNIVERSITY OF COLORADO
BOULDER, COLORADO

Economics 4413
International Trade

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<u>Office Hours</u>: Monday, Wednesday, 9:30-11:00

Course Outline and Reading List

The Course Outline given below lists the major topics we will deal with in this course. Markusen et.al. is the textbook. This textbook is currently out of print pending a revision. I have made copies of the whole book and will sell them at copying costs.

Copies are available at the Ink Spot copy center in Norlin Library (not the one in the UMC). They will make limited copy runs, starting with 20 copies so as to not lose money on the deal. After those are sold out, you can order one by visiting or calling the center at 2-7388, and they have promised that you will get a copy in 24 hours.

Markusen, Melvin, Kaempfer, and Maskus, *International Trade: Theory and Applications*, McGraw Hill, 1995.

Bhagwati, *In Defense of Globalization*, Oxford, 2004.

Assessment in the course will consist of:

1st mid-term exam	25%	Monday October 2
2nd mid-term exam (*date subject to change*)	25%	Monday November 6
Take home on *Globalization*	25%	Monday November 27 at *latest*
Final Exam	25%	Tues Dec 19, 10:30-1:00

<u>Late penalty on take home: 5% of total essay marks per day</u>

The exams will be analytical-essay type exams in which you will be asked, for example, to analyzed the relationship between two variables or assess the likely effects of some policy.

The book Globalization gives you a chance to learn about the practical links between economics and the globalization controversies currently debated around the world. The take-home exam will give you a set of essay questions which you will answer. The final exam and/or mid-terms will include some fill-in-the-blanks questions about the book to help insure that you actually read it!

In the lectures, I will try to present theory in the first half of the class period, and applications in the second half.

PART I: TECHNICAL TOOLS AND THE GAINS FROM TRADE

In this part of the course, we develop and review basic tools of microeconomic theory that we will use throughout the course.

1. Supply and Production Possibilities
   MMKM, Chapters 1 and 2.

2. Preferences, Demand, and Welfare
   MMKM, Chapter 3.

3. General Equilibrium in Open and Closed Economics
   MMKM, Chapter 4.

4. The Gains from Trade
   MMKM, Chapter 5.

PART II: DETERMINANTS OF TRADE

This section analyzes the different underlying causes of international trade and the gains from trade.

1. Differences in Technology between Countries.
   MMKM, Chapters 6 and 7.
   Skip section 5, chapter 7.

2. Differences in Factor Endowments between Countries.
   MMKM, Chapters 8 and 9.
   Skip section 6, chapter 8.

3. Government Policies as Determinants of Trade.
   MMKM, Chapter 10.
   Skip sections 4 and 5.

4. Imperfect Competition as a Determinant of Trade.
   MMKM, Chapter 11.
   Skip section 4.

5. Increasing Returns to Scale.
   MMKM, Chapter 12.
   Skip sections 5 and 6.

6. Preferences and Income as Determinants of Trade.
   MMKM, Chapter 13.

PART III: TRADE POLICY

This part of the course analyzes the principal tools that governments use to influence trade. We analyzed the effects of the policies and try to understand the reasons that governments choose the policies they do.

1. Tariffs
   MMKM, Chapter 15.
   Skip section 7.

2. Quotas
   MMKM, Chapter 16.
   Skip section 5.

3. Imperfect Competition, Increasing Returns, and Strategic Trade Policy.
   MMKM, Chapter 17.
   Skip section 4.

4. Preferential Trade Areas
   MMKM, Chapter 18.
   Sections 1 and 2 only.

5. The Political Economy of Trade Policy
   MMKM, Chapter 19.

PART IV: FACTOR TRADE AND DIRECT FOREIGN INVESTMENT

The final section of the course looks at trade in factors of production and direct foreign investment be multinational firms.

1. Trade in Factors of Production
   MMKM, Chapter 21.
   Skip sections 2 and 5.

2. Direct Foreign Investment
   MMKM, Chapter 22.
   Skip section 4.

3. Intertemporal Trade
   MMKM, Chapter 23.
   Section 1 only.

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International Trade - Review/Sample Questions

1. Suppose that there are two goods, X and Y, and only one factor of production L. Assume that Y is produced with constant returns and X is produced with increasing returns. Explain the shape of the production possibilities frontier. What the significance of this shape for trade?

2. The balance-of-trade condition is equivalent to the condition that the value of a country's production equals the value of its consumption. True/false, explain.

3. Two countries can gain from trade even if one country has an absolute advantage in the production of all goods. True/false, explain.

4. Construct one careful example to show how one individual can lose from trade even if the country as a whole gains from trade relative to autarky. Does this help us understand controversies over trade liberalization?

5. The free-trade price ratio must lie between the autarky price ratios of the two countries. True/False, explain.

6. State the factor-price equalization theorem. What is its implications for the wage of unskilled labor in the US following trade liberalization?

1. Government policies can induce trade or reverse the direction of trade, but such trade is not necessarily beneficial. True, False, explain.

2. Production and consumption taxes tend to have opposite effects on the direction of trade. True, False, explain.

3. Define the concept of pro-competitive gains from trade and give an example of when they might arise.

4. "Gains from trade in the presence of scale economies can be taken either in the form of the same number of products at lower prices, or more products at the same prices." Explain this statement.

5. State the "Linder Hypothesis". What empirical facts are this theory suppose to explain? Why can't the Heckscher-Ohlin model explain these facts?

1. Under what circumstance is the effect of an import quota the same as the effects of an import tariff?

2. What is "quota rent" and how is it distributed in a quota that is auctioned off versus a voluntary export restraint?

3. Analyze the effect of an export subsidy (assume perfect competition, no distortions).

4. Discuss briefly the intuition behind the argument that a country's welfare may be improved by a production or export subsidy for an industry producing with increasing returns and imperfect competition.

5. Present alternative assumptions to those in question 3 such that we arrive at the conclusion that a subsidy is welfare worsening.

6. What is the argument underlying "import protection as export promotion"? What is assumed about production?

7. State the "theory of the second best". In what way does it underlay the concept of strategic trade policy?

8. Explain "trade creation" and "trade diversion". How was this relevant to Mexico in evaluating NAFTA?

9. Discuss in what sense trading goods and trading factors are equivalent.

10. Present a situation in which trading goods and factors are in some sense complements.

11. Outline the OLI view of multinational firms. What are the principal sources of ownership advantages for multinational firms?

12. Discuss the reasons why multinational firms are closely associated with knowledge capital or knowledge based assets.