

Economics 475  
D.H. Feldman, Fall 2018  
email: [dhfeld@wm.edu](mailto:dhfeld@wm.edu)  
appointment.

Office: 266 Tyler  
Hours: T, Th, 9:00 – 10:00, and F, 2:00 – 3:00  
or by

## International Trade: Theory and Policy

Text: *International Trade: Theory and Policy*, by Krugman, P., Obstfeld, M., and Melitz, M. (Pearson, 2018). Eleventh Edition. *At Bookstore. Henceforth called KOM.*

NOTE: You may also use the tenth, or even the ninth edition. They will be cheaper. The book we're using is the "split" version that only covers the trade material. Some of you may obtain the complete hard back (which includes the macro side) called International Economics: Theory and Policy. That's fine too. If you acquire the MyEconLab program along with it, that will give you lots of extra practice stuff to do, but it's not at all required.

Some Helpful but Optional Reading:

Drezner, D., The Irony of Global Economic Governance: The System Worked, IIGG Working Paper, October 2012. [On Blackboard under Course Documents.](#)

## Course Outline

### **I. Introduction to World Trade**

- Basic patterns of world trade
- The Gravity Model
- The WTO and the institutional structure of world trade.

Reading: KOM, chapters 1-2.

Are You Open: an interactive map from the St. Louis Fed. [On BB in External Links.](#)

The WTO in Brief (all four sections). [On Blackboard in External Links.](#)

Dynarski, Susan. For Better Learning in College Lectures. [On Blackboard under Course Documents.](#)

Worthen, M., Lecture Me – Really! [On Blackboard under Course Documents.](#)

Op-eds by Krugman (Gravity), and Rodrik. [On Blackboard under Op-Ed Documents](#)

Dynarski and Worthen address best practices in learning. They are not writing about international trade. Read what they have to say. Their arguments and evidence reflect my thinking as well. Worthen's op-ed also introduces you to the op-ed as a form of writing. You will write one in this class. The pieces by Krugman and Rodrik are examples of very current trade-related op-eds.

### **II. Trade Theory in Competitive Markets**

#### **A. Comparative Advantage in the Ricardian Model**

- The gains from trade
- The Terms of Trade

- Some common myths
- traded and non-traded goods
- An infinite-goods version of the Ricardian Model

**Reading:** KOM, chapter 3.

Krugman, P., "What do Undergrads Need to Know About Trade," *American Economic Review*, 83 (May 1993), 23-27. [On Blackboard in Course Documents \(PDF file\)](#)

Feldman, D. "Ricardian Model with N Goods." [On Blackboard in Course Documents.](#)

#### **Problem Set: 1**

*An Extension: Why are price levels lower in developing countries? or, a dollar sure is worth more in Delhi than in Duluth.*

Reference: The Penn World Table. [On Blackboard in External Links.](#)

*An Extension: Trade, the environment, and social collapse.*

**Reading:** Diamond, Jared, *Paradises Lost*, *Discover Magazine*, November 1997. [On Blackboard in External Links.](#)

### ***First Quiz: Friday, September 21<sup>st</sup>***

#### **B. Specific Factors, Trade, and the distribution of income**

- Factor mobility and the gains from trade (an immobile factors model)
- Winners and losers: why free trade does trade **NOT** benefit everyone?

**Reading:** KOM, chapter 4

Further Reading:

Autor, Dorn, and Hanson (2016). The China Shock: Learning from Labor Market Adjustment to Large Changes in Trade. <https://www.ddorn.net/papers/Autor-Dorn-Hanson-ChinaShock.pdf>

Gary C. Hubauer and Zhiyao Lu, "The Payoff to America from Globalization: A Fresh Look with a Focus on Workers, Peterson Institute for International Economics, Policy Brief 17-16, May 2017. *Zhiyao (Lucy) Lu sat in this class not too many years ago.*

#### **Problem Set: 2**

#### **C. Resources: the Heckscher-Ohlin model and the Standard Trade Model**

- Relative factor abundance and the pattern of trade
- Winners and losers again: Factor Price Equalization and the Stolper-Samuelson theorem
- Changes in factor endowments: The Rybczynski theorem.
- The Standard Trade Model: growth and the terms of trade.

**Reading:** KOM, chapters 5-6.

**Problem Set: 3.**

*An Extension: Economic Sanctions*

**Reading:** Davis, Lance, and Engerman, Stanley, “Sanctions: Neither War Nor Peace,” *Journal of Economic Perspectives*, 17 (Spring 2003), 187-97. [On Blackboard in Course Documents \(PDF file\).](#)

**FIRST EXAM: Friday, October 12<sup>th</sup>**

**SPRING BREAK**

**III. Returns to Scale and Global Economic Integration.**

**A. External Economies of scale and the pattern of trade**

- The geographic location of industries.
- Historically determined trade patterns and the role of accident.
- International trade, and interregional trade.

**Reading:** KOM, chapter 7.

**B. Internal Scale Economies and Firms in the Global Economy**

- Monopolistic Competition in Differentiated Products
- Intra-industry versus inter-industry trade and the distribution of income
- Heterogeneous firms: the Melitz Model.
- Trade and Productivity, the role of exports.
- Dumping

**Reading:** KOM, chapter 8, up to 196, plus appendix (p. 214).

Feldman, D., “The Monopolistic Competition Model.” [Under Course Documents: Lecture Notes. This is all of the algebra, paired with the geometry.](#)

**Problem Set: 4**

**C. Outsourcing and Multinationals**

**Reading:** KOM, chapter 8, pp 197 – end of chapter.  
Bhagwati, J., Panagariya, A., and Srinivasan, T.N., “The Muddles over Outsourcing,” *Journal of Economic Perspectives* 18 (Fall 2004), 93-114. [On Blackboard in Course Documents \(PDF file\).](#)

**Further Reading:**

Irwin, Douglas: “Outsourcing is Good for America,” AEI, February 2004.

Mann, Catherine: "Globalization of IT Services and White Collar Jobs: The Next Wave of Productivity Growth," IIE Policy Briefs, PB03-11, December 2003.  
Bureau of Labor Statistics, Occupational Employment Statistics. The raw data on employment by occupation is here: <http://www.bls.gov/oes/home.htm>

#### **D. International Migration**

- The Benefits and Consequences of Immigration
- The other side of the looking glass: emigration

**Reading:** KOM: Reread chapter 4, pp. 72-78. This is where labor mobility first appears in KOM.  
Borjas, George J., "The Economic Benefits of Immigration," *Journal of Economic Perspectives*, 9 (Spring 1995), 3-22. [On Blackboard in Course Documents \(PDF file\)](#).

Clemens, Michael, "Economics and Emigration: Trillion Dollar Bills on the Sidewalk?" *Journal of Economic Perspectives*, 25 (Summer 2011), 83-106. [On Blackboard in Course Documents \(PDF file\)](#).

#### **Further Reading:**

Freeman, Richard B., "People Flows in Globalization," *Journal of Economic Perspectives*, 20 (Spring 2006), 145-170. [On Blackboard in Course Documents \(PDF file\)](#).

***Op-Ed Due: Friday, November 19<sup>th</sup> at 5:00 P.M.***

### **IV. Commercial Policy and the Politics of Trade Policy**

#### **A. Economic implications of tariffs and quotas**

- How do Tariffs and Quotas Work?
- The welfare effects of commercial policies
- non-economic objectives,
- tariff equivalence propositions
- measurement of costs
- the Effective Rate of Protection
- How do trade policies affect price uncertainty, and how does uncertainty affect the trade policies we get?

**Reading:** KOM, chapter 9, with appendix.

#### **Problem Set: 5**

#### **B. Principles of "optimal" policy**

- externalities and the hierarchy of policies (the by-product distortion)
- tariffs to generate government revenue: The Maximum Revenue Tariff
- Infant industry protection (dynamic returns)
- the "optimal" tariff for a large country, i.e. market power in trade.

**Reading:** KOM, chapter 10 from 246-254, and appendix.

## **Problem Set: 6**

### **Further Reading:**

Corden, W.M., *Trade Policy and Economic Welfare*, Oxford: Clarendon Press, 1974.  
Chapters 2-4. [Many lectures are drawn from this material] [On Blackboard in Course Documents \(PDF file\)](#).

## **C. The Political Economy of Trade Policy**

### **1. Income Distribution and Trade Policy**

- Rent-Seeking
- Self-interest and the role of interest groups
- Endogenous Policy Theory
- The China Shock

**Reading:** KOM, chapter 10, pp. 255 – 259.

Look at Autor, Dorn, and Hanson's website: <http://chinashock.info>

### **2. Administered Protection and Declining Industries**

- The International Trade Commission
- Anti-Dumping, Safeguard, and Countervailing Duty processes.
- Trade Adjustment Assistance

Hufbauer, Gary C., and Goodrich, Ben, "Steel Policy, the Good, the Bad, and the Ugly," Institute for International Economics, Policy Brief PB03-1, January 2003.  
[On Blackboard in Course Documents \(PDF file\)](#).

Kletzer Lori G., and Litan, Robert, "A Prescription to Relieve Worker Anxiety," Institute for International Economics, Policy Brief PB01-02, January 2001.  
[On Blackboard in External Links](#)

### **3. International Negotiation and the World Trade Organization**

- From the GATT to the WTO
- Rationales for multilateral negotiation: the case for MFN
- Rules and dispute mechanisms
- Preferential Trade Areas and Agreements (like the EEC, NAFTA, MERCOSUR).

**Reading:** KOM, chapter 10, pp. 260 – end.

## **Problem Set: 7 (maybe)**

***Second Exam: Friday, November 30<sup>th</sup>.***

## **V. The Global System: Current Controversies**

## A. The "New International Economics" and Activist Trade Policy

- Scale economies and "strategic" sectors.
- Duopoly and other game theoretic approaches.
- Problems with strategic trade policy

**Reading:** KOM, chapter 12, pp. 298 – 306.

BBC video: [Why the Airbus 380 Never Really Took Off](#). Also on BB under Readings Available as Links.

“The Airbus Showdown,” by Robert Samuelson. *Washington Post*, December 8, 2004. [On Blackboard in Course Documents](#).

### Further Reading:

Irwin, D, and N. Pavcnik (2004). “[Airbus versus Boeing revisited: International Competition in the Aircraft Market](#)”. *Journal of International Economics*; V.64-#2, pp. 223-245.

## B. Trade, the Environment, and Standards

- Competition for industries: A race to the bottom?
- Cross-border externalities and the global commons
- process vs. product
- the role of the WTO

**Reading:** KOM: Chapter 12, pp. 307 – end.

The Environment -- A New High Profile. [On Blackboard in External Links](#).

Bagwell, K, and Staiger, R., “The WTO as a Mechanism for Securing Market Access Property Rights, Implications for Global Labor and Environmental Issues,” *The Journal of Economic Perspectives*, 15 (Summer, 2001), 69-88. [On Blackboard in Course Documents \(PDF file\)](#).

Brown, D., “Labor Standards: Where do they Belong on the International Trade Agenda?” *The Journal of Economic Perspectives*, 15 (Summer, 2001), 89-112. [On Blackboard in Course Documents \(PDF file\)](#).

### Further Reading:

Bhagwati, J., and Srinivasan, T.N., "Trade and the Environment: Does Environmental Diversity Detract from the Case for Free Trade," *Fair Trade and Harmonization: Prerequisites for Free Trade?*, Cambridge: MIT Press, 1996) [\[More Technical, and quite provocative. From the book Krugman reviews\]](#)

Corden, W. Max, *Trade Policy and Economic Welfare*, ch. 13 “Trade Policy and the Environment,” 2<sup>nd</sup> edition, Oxford: Oxford University Press, 1997.

# ***Final Exam (Quiz): December 11<sup>th</sup> at 2:00 P. M.***

## **EVALUATION:**

You will have four major assignments this semester. The first is a quiz that follows the Ricardian model. This quiz is a gentle introduction to my tests, and it helps you to prepare for the first exam that follows

section II. The quiz is worth 12% of your grade. We will have two midterm exams. Each is worth 33% of your grade. You will see these listed on the syllabus after sections II and IV of the course. The second midterm will take place on the last day I'm allowed to give an exam (Friday, April 20<sup>th</sup>). The "final examination" is optional, hence the quotes. It will be structured like the first quiz and is designed to be doable in 30 minutes. It will be comprehensive, i.e. drawn from models throughout the class. If you do better on this "final" than on the first quiz, I will replace the lower mark with the higher mark. If your worst mark is on one of the exams instead of the first quiz, I will replace 1/3 of the value of the offending exam with the points from the final quiz. This is a small bonus for improvement or a small reward for the extra work done to repair the damage from a less than stellar day. Do not count on the final quiz to radically alter your course grade. That is statistically very unlikely. In fact, if you are not near a grade borderline, your best choice may be to skip my final "quiz" and reallocate your time toward another class's exam or final paper where the marginal gain to you from your efforts may be substantially higher.

We will also have one short "paper" in the class. Given the contemporary populist buzz about most things global/international, I'm asking you to write a 750 word op-ed on some trade or trade policy issue. I have posted my own writing hints along with a great op-ed by Bret Stephens in the NY Times on how to write op-eds! This is an especially important writing assignment despite its extreme brevity. A 750 word essay is actually far more difficult to build than a 5-10 page paper. An op-ed with fluff is an op-ed that says very little. You can't hide a weakly written argument in that short a space. Every word counts. This is a paper that should be drafted early in the course and then carefully redrafted several times as you learn more about the issues and as you rethink your argument or you're your sentence structure. Like the first quiz, the op-ed will be worth 12% of your grade. It is due by 5:00 P.M. on Friday, November 19<sup>th</sup> at the latest. You can turn it in much earlier if you want to get it out of the way!

The remaining 10% of your grade is based on a number of other things. The first is attendance and participation. If you are not in class you are much less likely to master the complex models we build to explain global trade. Attendance is objective, and participation is subjective. I'm the judge of the latter. The attendance/participation is 5%. That may not seem like a large amount, but it could mean the difference between a C+ and a B-. The remaining 5% comes from a set of short problems that you will solve and turn in online. These can be turned in individually, or collectively from your study group. More on study groups in the next paragraph. When I post the questions, you will have a short amount of time (a few days) to complete the question or questions, and submit them on Blackboard. These problems will be good practice for the quizzes and exams.

I have also prepared a series of larger problem sets as homework assignments. The ones from last semester are in place, and I will update them and change them as we go along. You will notice that they are non-graded. The answers are already there too. That does not mean the problem sets are unimportant. You will have real difficulty completing the online questions, the quizzes, and the exams, if you don't spend quality time working on these extended homework assignments. They are a crucial part of mastering the models that we use to explain global trade, national trade policy, and the institutional structure of trade. You should sort into study groups to work on these problem sets. Limit the number of people in your group to a maximum of four to ensure that shirking is reduced to a bare minimum. Use the study groups for more than just the problem sets! Meet several times per week to discuss the course and to argue about facts, theory, and policy. And make sure you work on problem sets continuously instead of trying to cram them into your head just before the exams. If you wish, I can help you set up a place on the Blackboard site so that you can communicate within your group about problem sets, or about anything class related. I encourage people to post questions about the material to open class forums, and I will reward people who volunteer time to help un-confuse the bewildered. This is another way to earn class participation kudos.

We have a TA for the class. Her name is Alexis Payne. She has taken this class. She understands your pain (bad pun, bad pun). Alexis will hold open hours once or twice per week. I will add that information to the syllabus when it's finalized. Please keep Alexis very busy. Do not wait to utilize her help until the week

before a test or quiz. Whenever you have questions from class notes, the text, or from problem sets, talk to her or to me in a timely fashion. Come as a group as well. That way everyone in the group will benefit from every other group member's questions.

**Additional Information: Alexis's TA sessions will take place every .... (I'll fill this in when I know).**

**From the Student Accessibilities Service Office:**

"William & Mary accommodates students with disabilities in accordance with federal laws and university policy. Any student who feels s/he may need an accommodation based on the impact of a learning, psychiatric, physical, or chronic health diagnosis should contact Student Accessibility Services staff at 757-221-2509 or at [sas@wm.edu](mailto:sas@wm.edu) to determine if accommodations are warranted and to obtain an official letter of accommodation. For more information, please see [www.wm.edu/sas](http://www.wm.edu/sas) "

**From the Dean of Students and the Honor Council:**

"The College of William & Mary has had an honor code since at least 1779. Academic integrity is at the heart of the College, and we all are responsible for upholding the ideals of honor and integrity. The student-led honor system is responsible for resolving any suspected violations of the Honor Code, and I will report all suspected instances of academic dishonesty to the honor system. The Student Handbook ([www.wm.edu/studenthandbook](http://www.wm.edu/studenthandbook)) includes your responsibilities as a student and the full Code. Your full participation and observance of the Honor Code is expected. To read the Honor Code, see [www.wm.edu/honor](http://www.wm.edu/honor)"

**From Sharon Zuber of the Writing Center:**

The Writing Resources Center, located on the first floor of Swem Library, is a free service provided to W&M students. Trained consultants offer individual assistance with writing, presentation, and other communication assignments across disciplines and at any stage, from generating ideas to polishing a final product. To make an appointment, visit the WRC webpage [www.wm.edu/wrc](http://www.wm.edu/wrc).

The WRC opens for the Spring semester on Monday, January 29th.

Questions? Contact Sharon Zuber at [slzube@wm.edu](mailto:slzube@wm.edu) or Lori Jacobson at [ljacobson@wm.edu](mailto:ljacobson@wm.edu).