

Economics 475  
D.H. Feldman, Fall 2016  
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Office: 266 Tyler  
Hours: T, Th, F 9:00 – 10:00,  
or by appointment.

## *International Trade: Theory and Policy*

Text: *International Economics: Theory and Policy*, by Krugman, P., Obstfeld, M., and Melitz, M. (Addison Wesley, 2014). Tenth Edition. **At Bookstore. Henceforth called KOM.**

**NOTE: You may also use the ninth edition. It's cheaper. Also, there are "split" versions that only cover the trade material ... cheaper still!**

Interesting Optional Background Accompaniments: (available in the Library or through Amazon etc).

*Fair Trade for All*, by Joseph E. Stiglitz and Andrew Charlton, (Oxford: Oxford University Press, 2005). **A critique of global institutions.**

*Trade Policy Disaster: Lessons from the 1930s*, by Douglas A. Irwin, (Cambridge: MIT Press, 2011).

## 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.

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

Drezner, D., The Irony of Global Economic Governance: The System Worked,

IIGG Working Paper, October 2012. [On Blackboard under Course Documents.](#)

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

Op-eds by Summers, and Wright & Blanchard. [On Blackboard under Op-Ed Documents](#)

### **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: Monday, September 18<sup>th</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 13<sup>th</sup>***

**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.
- International trade, and interregional trade.

**Reading:** KOM, chapter 7.

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

- Monopolistic Competition
- Intra-industry versus inter-industry trade
- Heterogeneous firms and how firms respond to trade
- Dumping

**Reading:** KOM, chapter 8, up to 180, plus appendix (p. 205).

**Problem Set:** 4

**C. Outsourcing and Multinationals**

**Reading:** KOM, chapter 8, pp 190 – 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. 69-73. 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 \(PDF file\)](#).

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

***Op-Ed Due: Friday, November 17<sup>th</sup>***

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

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

- welfare effects of commercial policy
- non-economic objectives
- tariff equivalence propositions
- measurement of costs
- effective protection
- role of uncertainty

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

**Problem Set: 5**

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

- externalities and the hierarchy of policies
- tariffs to generate government revenue
- Infant industry protection
- the "optimal" tariff for a large country

**Reading:** KOM, chapter 10 from 219-229, 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. 229-234.

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 9 (pages 234-247).

**Problem Set: 7 (maybe)**

***Second Exam: Friday, December 1<sup>st</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. 271-279.

"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 (pages 279-290).

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 12<sup>th</sup> at 9:00 A.M.***

### **EVALUATION:**

You will have four required 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 (following section **II**). The quiz is worth 12% of your grade. We will have two midterm exams. Each is worth 36% 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, December 1<sup>st</sup>). The "final examination" is optional, hence the quotes. It will be structured like the first quiz (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. 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. If you are the rare person who aces the quiz but performs significantly less well on one of the bigger exams, I will average the final quiz together with your lowest exam in a ¼ ratio (like their relative weight), which could pull up your lowest exam score a bit. 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 border line, 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 may be substantially higher.

We will also have one short “paper” in the class. Given the contemporary populist buzz against 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 on November 11<sup>th</sup>.

The remaining 4% of your grade is based on attendance and participation. Attendance is objective, and participation is subjective. I’m the judge of the latter. This 4% may not seem like a large amount, but it could mean the difference between a C+ and a B-.

I have prepared a series of 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. 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.

### **Additional Information:**

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)"