

EC 380: Lecture 1

Intro to International Economic Issues

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Winter 2022

Prologue

Course Objectives

For this class we will:

- study baseline models explaining why countries trade
- analyze policy-relevant trade tools (tariffs, quotas, subsidies)
- explore global finance through exchange rates and BoP

Course Objectives: Synergies



Today's Plan

1. **Course logistics**
2. About me
3. Key facts about international trade
4. If time allows... overview of key models of trade

Course logistics

We will use **(IE)** while latter text is completely optional:

- International Economics by James Gerber **(IE)** 7th-8th Ed.
- International Economics by Feenstra & Taylor **(IE)** 3rd-5th Ed.

Content will be available on Canvas. If familiar with the platform, see the course **Github** page.

- **W1-W3:** Theory of Trade
- **W4-W7:** Trade Policy
- **W8-W10:** Global Finance
- 25% - 5 Problem Sets
- 10% - 3 Quizzes, best 2
- 25% - Midterm Exam
- 40% - Final Exam

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About me

Philip Economides

- Currently: PhD Candidate, Economics, Teaching Int. Trade, Int. Econ and Econometrics
- Previously: RA at ESRI/Trinity College Dublin, Ireland
- Focus: International Trade, Transport Economics, Applied Econometrics

Where can you find me?

- Online Office hours: Tuesday 15:00-16:00, Thursday 10:00-11:00, or by appointment
- Email: peconomi@uoregon.edu **(use EC 380 in the subject line)**

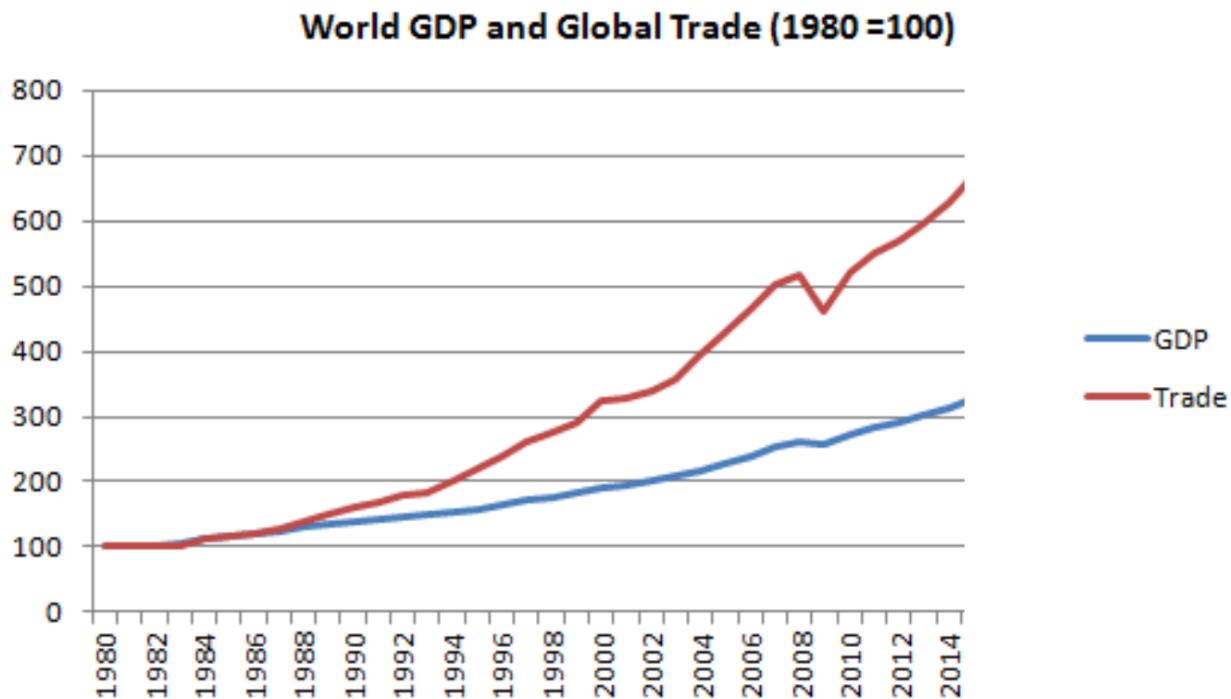
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International Trade:

Key Facts

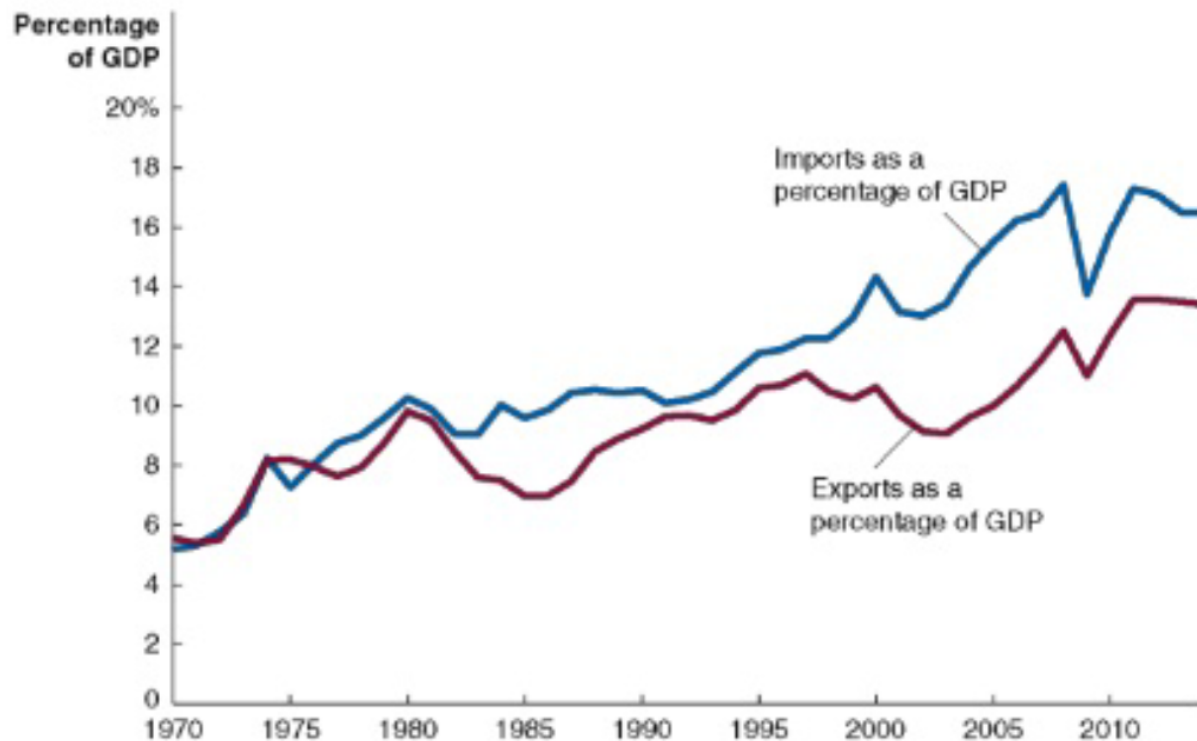
Trade growth outpaces GDP growth



Source: IMF World Economic Outlook (2012)

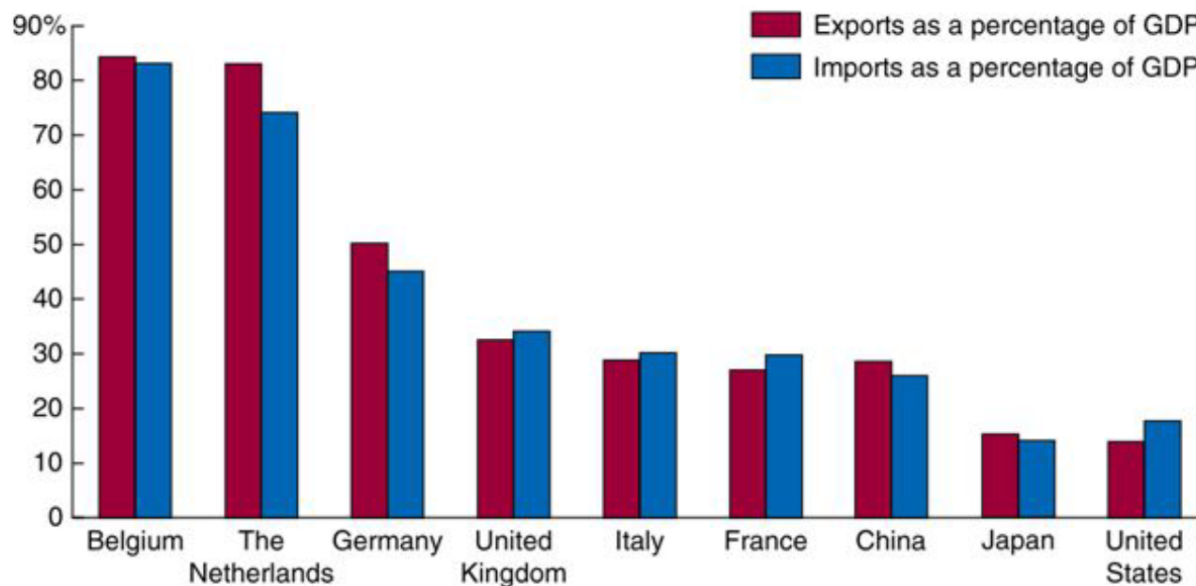
Recent slowdown in trade, which we will address

Flows rising as share of GDP (US)



Source: Hubbard and O'Brian (6th ed.)

Trade varies in importance



Source: Hubbard and O'Brian (6th ed.)

Small open economies are highly reliant on trade.

Key Facts I

- Trade is important and increasingly so
- Flows represent a large portion of US GDP
- Trade openness varies across countries of different sizes

Questions arise:

- Why do countries trade so much and why is it growing in scale?
- What are the gains from trade?
- How does trade translate into other changes (e.g. labor market outcomes, geopolitical tensions)

Part I of this course will focus on the **theories of international trade**. By the time we are done, very generalized lessons will be available to us.

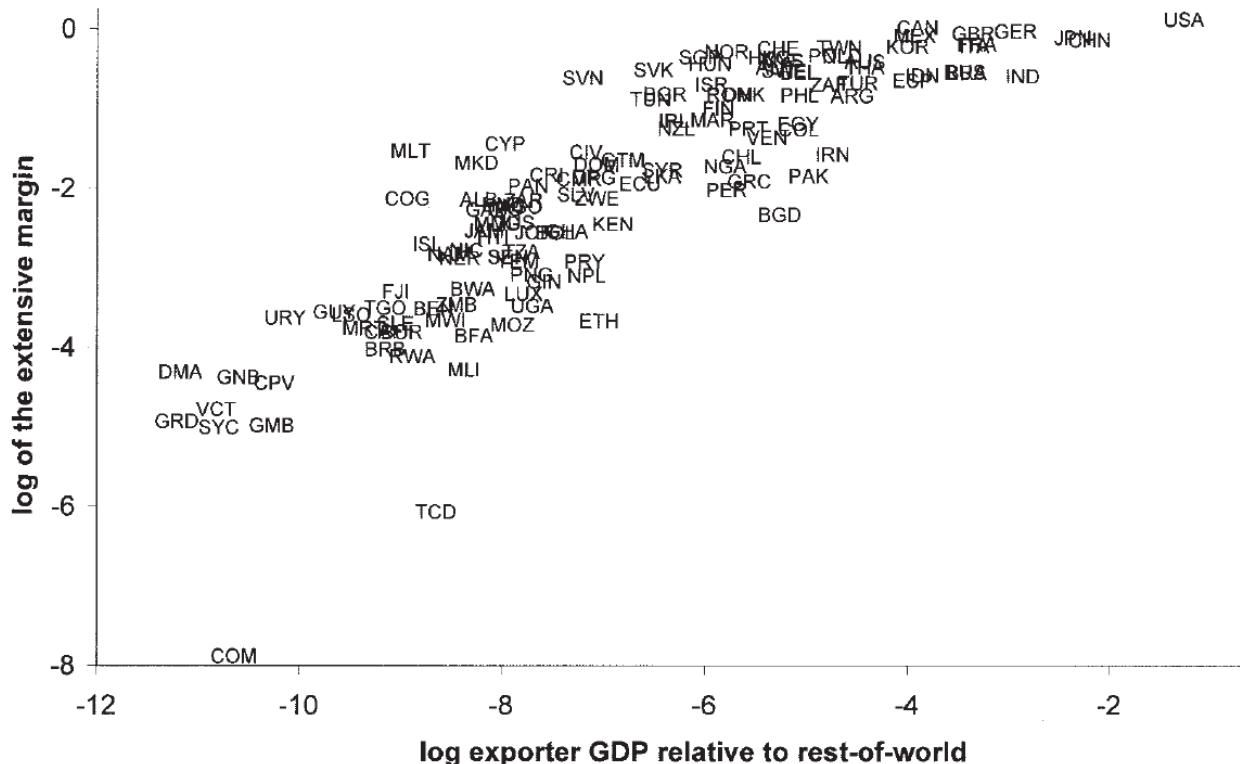
Introducing Theory

Main Questions:

- What goods do each country trade?
- How does trade affect product specialization?

What goods do each country trade?

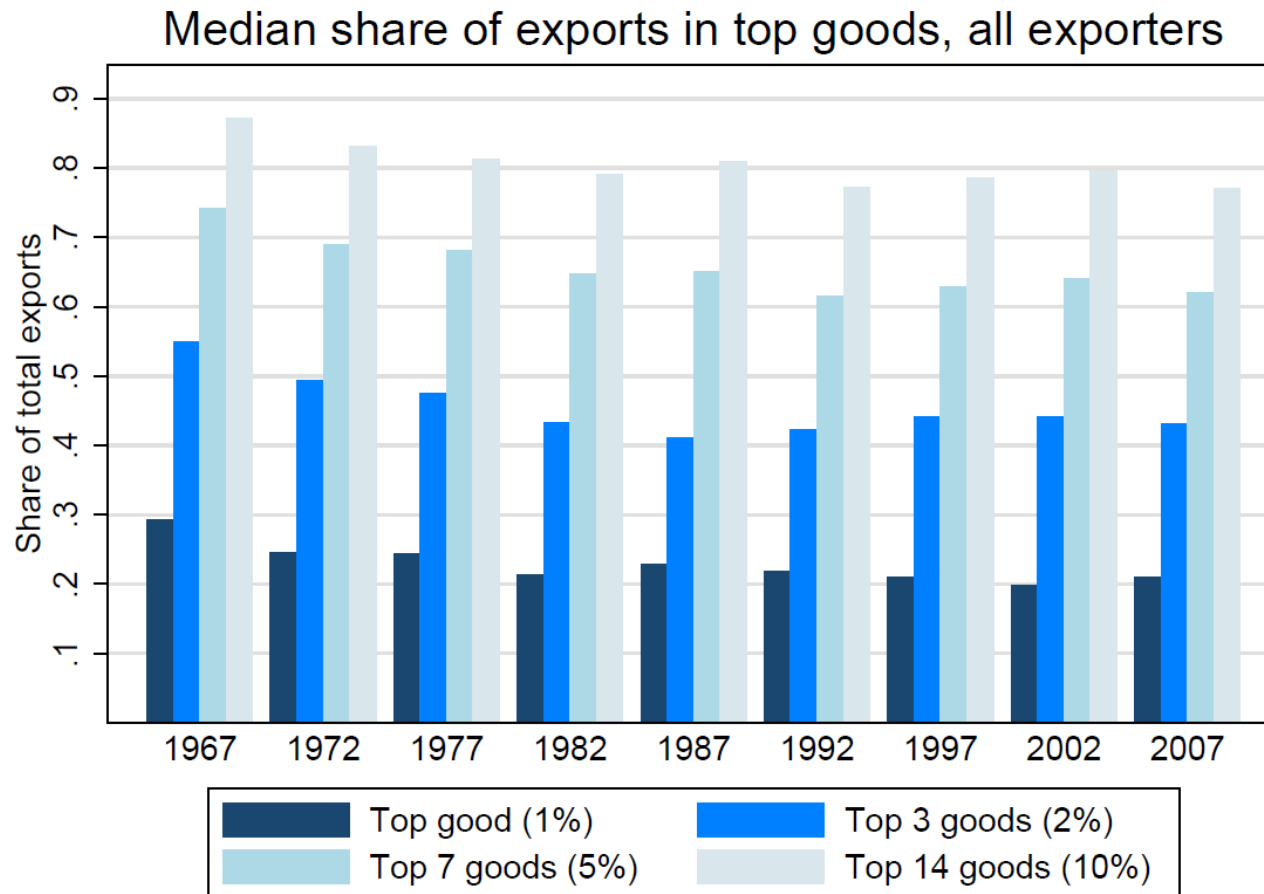
Product Range varies with Country Size:



Note: Product extensive margin (y-axis) is a weighted average count of the number of products a country exports in 1995.

Source: Hummels and Klenow (2005)

Specialization and Compar. Advantage



Notes: Sample includes 90 countries and 133 time-consistent industries.
Shares of industry i 's exports in total exports of country c are calculated by country.

Source: Hanson, Lind and Mender (2015)

Key Facts II

- Countries specialize and export core products
- Trading the goods that countries are "best" at producing results in *gains from trade*

What factors, other than fundamentals, influence specialization?

- Foreign direct investment (FDI)?
- Knowledge diffusion?
- Cross-border migration shocks?

Why does trade continue growing?

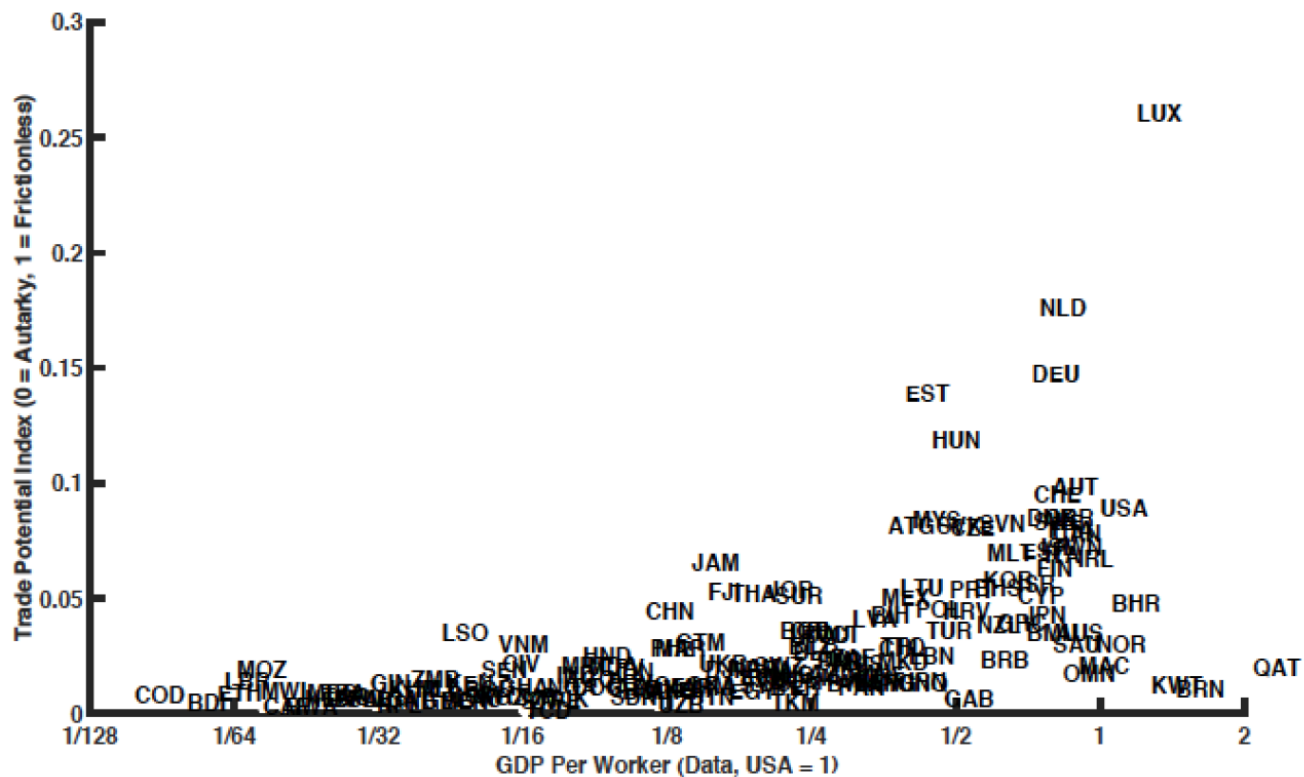
Largely attributed to reduced trade barriers over time.

We refer to this process as **trade liberalization**.

Examples include tariff rate reductions, preferential trade agreements and alleviating non-tarif measures (e.g. lower electronics quota for French imports to USA).

Since trade is not frictionless, do these frictions vary across countries?

Trade friction index



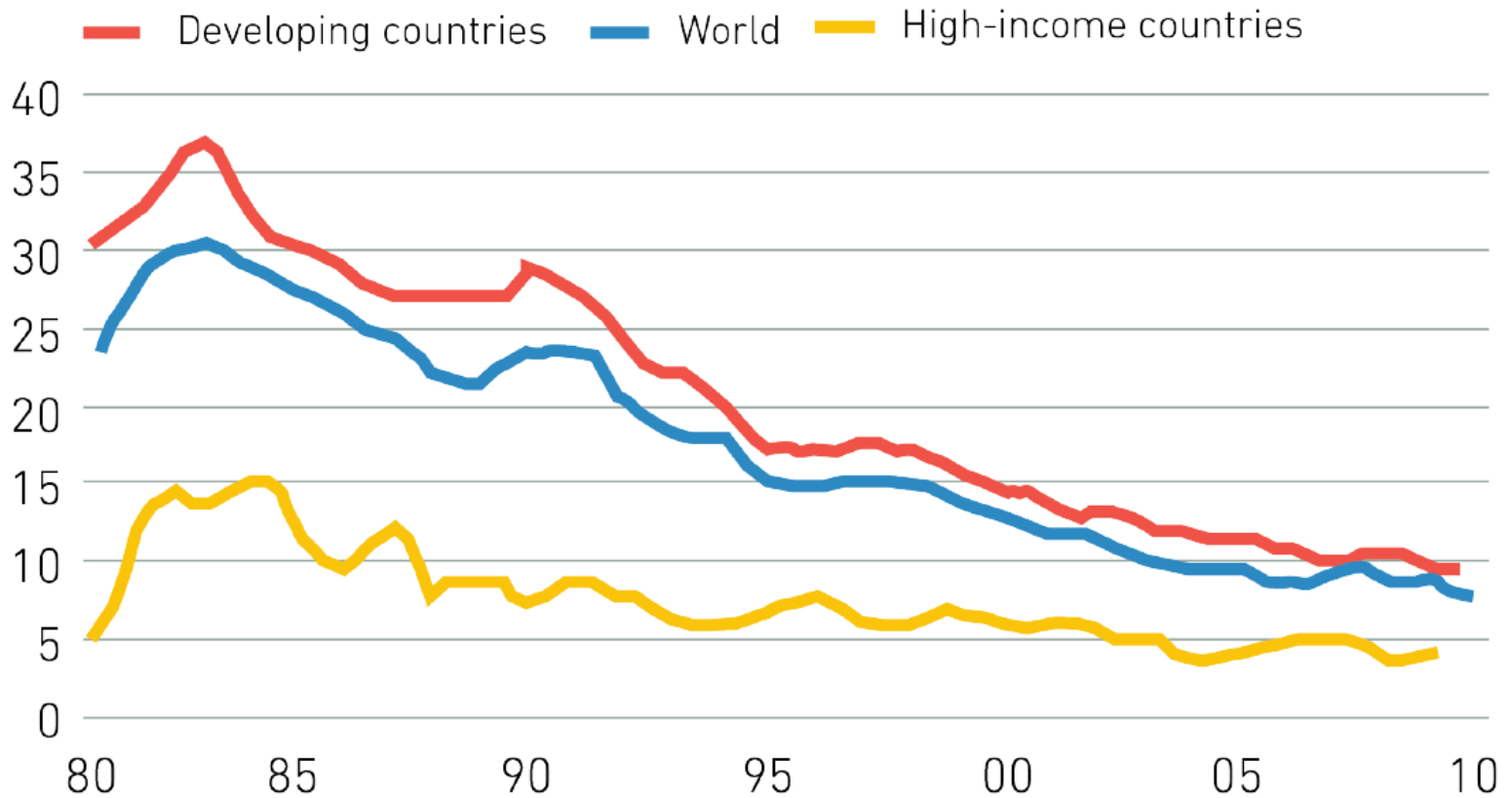
Trade Potential Index = index capturing a country's position between autarky (index = 0) and frictionless trade (index = 1)

Data for 2005

Source: Waugh and Ravikumar (2016)

Reduced Tariffs

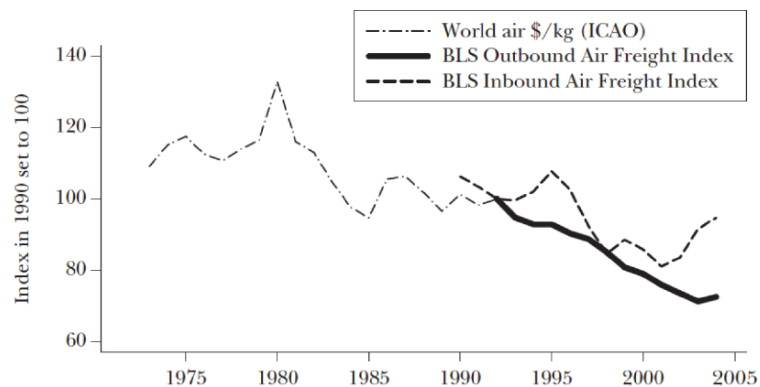
Trends in tariff rates (%)



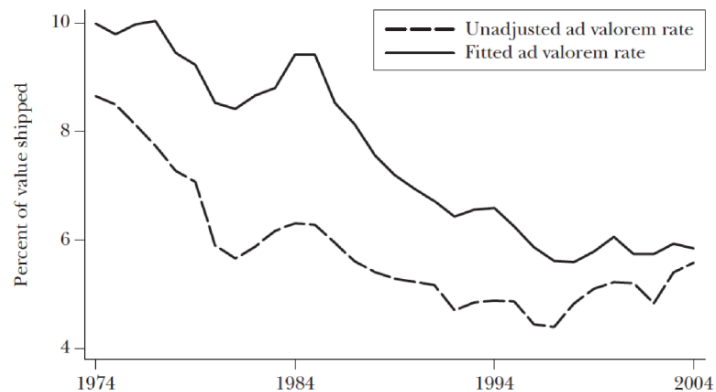
Source: World Bank

Lower Transport Costs

Air Transport Price Indices



Ad Valorem Ocean Freight



Source: Hummels (2007)

Key Facts III

- Explicit trade barriers have fallen over time, coinciding with the growth of trade relative to broad economic activity
- Hidden barriers are the next hurdle, one which much of the literature suggests is far more impactful than existing tariff rates

Current trade theory and literature focuses on **heterogenous agent models**, which was originally created to explain why not every firm functions as an exporter.

We **will not** be going that deep into international trade, though I can recommend some texts for those interested in understanding the most modern forms of theory.

Overview Trade Theory

Why does trade occur? Two strands within the field of international trade:

I. Neoclassical models of trade ('old' theories):

- Ricardian model: Technology differences spur trade
- Heckscher-Ohlin model: Resource differences spur trade

II. 'New' Trade Theory

- Krugman model: Love of variety spurs trade
- Melitz model: Heterogenous firms drive trade

Next Class

We will begin looking into international trade theory, starting with the **Ricardo model**.

- Single factor of production (labor)
- Two-country model (home, foreign)
- Technology differences across countries

Going forward, try to describe each model by three attributes, such as those listed above, and the model's main takeaway(s)!

Readings: International Economics, Ch.1: Introduction to the World Economy