INTERNATIONAL ECONOMICS I 2011-21213
UPF

Language of Instruction: English
Course Meeting times and place: Mondays and Tuesdays 10.30-12.00, Campus Ciutadella.
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Contact Hours: by appointment

Course Description

This course will follow closely

Krugman P., M. Obstfeld, and M.J. Melitz, *International Economics: Theory and Policy*. 9th. Edition. Pearson and Wesley, 2012.

The main material of the course corresponds to the chapters marked with three stars below, and is naturally grouped in two parts,

I) TRADE THEORY AND POLICY

Part 1: International Trade Theory

1.Week
Review of Basic General Equilibrium
Chapter 2: World Trade: An Overview ***
2.Week
Chapter 3: Labor Productivity and Comparative Advantage: The Ricardian Model ***
Chapter 4: Specific Factors and Income Distribution ***
3.Week
Chapter 5: Resources and Trade: The Heckscher-Ohlin Model ***
Chapter 6: The Standard Trade Model ***
Home Reading:
Chapter 7: External Economies of Scale and the International Location of Production *
Chapter 8: Firms in the Global Economy: Export Decisions, Outsourcing, and Multinational Enterprises *

Part 2: International Trade Policy

4.Week
Chapter 9: The Instruments of Trade Policy ***
Chapter 10: The Political Economy of Trade Policy ***
5.Week
Chapter 12: Controversies in Trade Policy ***
Home Reading:
Chapter 11: Trade Policy in Developing Countries *

Tuesday 25th. First Midterm

II) EXCHANGE RATES AND MACRO POLICY

Part 3: Exchange Rates and Open-Economy Macroeconomics

5.Week
Chapter 13: National Income Accounting and the Balance of Payments ***
6.Week
Chapter 14: Exchange Rates and the Foreign Exchange Market: An Asset Approach ***
Chapter 15: Money, Interest Rates, and Exchange Rates ***
7.Week
Chapter 16: Price Levels and the Exchange Rate in the Long Run ***
Home Readings:
Chapter 17: Output and the Exchange Rate in the Short Run *
Chapter 18: Fixed Exchange Rates and Foreign Exchange *

Part 4: International Macroeconomic Policy

8.Week
Chapter 19: International Monetary Systems: An Historical Overview ***
Chapter 20: Optimum Currency Areas and the European Experience ***
9.Week
Chapter 21: Financial Globalization: Opportunity and Crisis ***
Home Reading:
Chapter 22: Developing Countries: Growth, Crisis, and Reform *

Tuesday 29th. November Second Midterm

The chapters marked with one star will be required reading, but will not be covered in the (theory) classes.

The pace of the course will be fast, practically one chapter per (theory) class (in other words, two chapters per week). Please note that this leaves very little room for prevarication. I do advise you to keep up-to-date reading the relevant chapters, preferably *before* the class in which they are meant to be covered.

WHAT IS THE COURSE ABOUT?

Trade Theory and Policy

The central question of trade theory is simply ‘Why do nations trade?. Starting out from this question, the theory moves on to characterize the pattern of international trade (which nation trades what with which other nation), and to evaluate the gains (and losses) from trade, as well as the implications of trade for growth, income distribution, competition, etc. Note that, in this first part, the focus is on ‘barter’, that is, trade not mediated by money.

Trade theory is really a kind of general equilibrium theory in which it is assumed that across nations goods are traded while (at least some) factors of production are completely inmobile. The key idea is ‘comparative advantage’, one of the really BIG IDEAS in economics which originated with the English economist David Ricardo at the beginning of the 19th century. The idea is that even if you are worse at producing everything than someone else, trade between you and that other producer will still take place because you will end producing the item you are relatively better at producing. By specializing in this way, both you and your trading partner will end up better off than either of you would be in autarky. As you will see, the reasoning involved is simple but not trivial. In fact, this is one idea many people have seriously difficulty assimilating.

What will you learn in this first part? Hopefully, it will be clear to you why there is a strong consensus amongst mainstream economists regarding the desirability of free trade. Practically all economists agree that trade is (almost always) good (specially for the poor, globaliphobia notwithstanding). This is the main message of the whole course. Naturally, the point is to understand why this is so, not just to parrot a slogan.

Exchange Rates and Macro Policy Coordination

To every physical exchange of goods there is always a financial counterpart. When you buy a book, you get the book (the physical part), and the bookseller gets some euros (or a lot, as you will find out if you buy the textbook for this course). Of course, that is not the end of the story. The bookseller will then use the euros to buy something else, say, food. In effect, indirectly, the book will have been exchanged for food. The fact that to bring about such an exchange a valuable piece of paper (the euro) was required is however crutial. Why? Because the supply of euros is determined by the government practically subject to no physical constraints (worth mentioning - euros are essentially costless pieces of paper). Even though the euro is essentially paper, do not underestimate its importance: If the government were to withdraw all euros in circulation or print too few as the economy grows, the physical exchange (here food for books) will probably be, if not impossible, very hard to bring about. This, as you might already know, is the starting point of the one big branch of macroeconomics, monetary policy.

Now, when dealing with *international* exchanges of goods, two kinds of paper will intervene, say, euros and pounds. If you buy the book from Amazon U.K., for example, you yourself might pay in euros, but the bookseller will have to convert those euros into pounds in order to finally buy what he or she wants in the UK. The issue specific to an international exchange from a monetary point of view is then, how is the price of euros in terms of pounds determined? In other words, what determines the exchange rate of euros for pounds?

Again, the answer is governments, but now, not one government on its own, but many simultaneously. This gives rise to a second question specific to international exchange, namely, how do governments coordinate their monetary policies? Note that if UK prints a lot of pounds while the US prints very few dollars, it is likely that the price of pounds in term of dollars will fall, and this in turn will affect the physical terms of trade (how many book units can be exchanged for how many food units).

As you might know, monetary policy is closely linked to fiscal policy via the government budget constraint (the government either prints money, borrows or taxes to finance its expenditures). This implies that determining how many euros to print is closely related to the government’s expenditure and taxing decisions (the other big component of macro), and thus, coordinating monetary policy is tantamount to coordinating macro policy, period. That such a coordination, even amongst close partners, is not a minor problem, is clearly illustrated by the current euro crisis.

How does this modify the main message from trade theory (‘Trade is Good’)? While monetary considerations introduce important qualifications, I think it is still fair to say that most economists do not think the introduction of money invalidates the basic conclusion. In other words, despite monetary frictions, trade is still (mostly) good, though managing it becomes harder.

Prerequisites: An intermediate course in Microeconomics, with a solid grounding in basic general equilibrium.

Course Evaluation

The course will be evaluated on the basis of

1) 4-6 Homeworks (20% all) (assigned every week, starting out from the 2nd.)
2) Two Midterm Exams (15% each) (25th oct. and 29th nov.)
3) Final Exam (50%) (as scheduled by the university)(the September exam will count just the same, 50%).

On the homeworks:

The homeworks will consist of two types of questions: 1) ‘Knowledge’ questions (simple questions meant to help you absorb key concepts); and, 2) Somewhat more elaborate ‘problem’ questions meant to help you learn to use the concepts and tools you have learned. This ‘problem’ questions will often be based on additional readings assigned in class (including the chapters marked with one star in the preceding list).

Each problem set will consist of 4-5 knowledge questions and 2-3 problem questions. The homework will be assigned Monday in the theory class, and must be handed-in at the beginning of the following practice session. It will be returned graded one week later at the start of the next practice class.

On the exams:

The first midterm will cover basic trade theory. The second midterm will cover only the remaining material, i.e., the monetary part of the course. The final will cover both parts of the course.

All exams will be fill-in/multiple-choice. Each midterm will have 5 questions each. Both midterms will be two hours exams, and will be returned graded one week later at the theory class following the exam.

Attendance

Students arriving more than ten minutes late to the class will not be admitted.

Grading

As usual, passing grade is 5 (on a scale of 10).

Additional Literature:

A very popular (in the U.S.) but rather conventional and narrow textbook is the following

Salvatore, D. (2007) International Economics, 9th ed. Wiley and Sons.

A relatively intensive course like the present one leaves little scope for in depth discussion of specific cases. A book I highly recommend you read if you want to take a closer look at how trade works in a case close to you (literally), is the following,

Rivoli, Pietra (2009) The Travels of a T-Shirt in the Global Economy, Wiley and Sons.

A really hard-nosed defense of free trade can be found in

Irwin, D. (2009) Free Trade under Fire, 3rd. edition, Princeton University Press.

What about the case against trade? Unfortunately, the case against has not been really well argued (perhaps because it is a weak case). Here is one version, by a well known non-economist, and associates,

Nader, Ralph (ed.) (1993), The Case Against Free Trade: Gatt, Nafta and the Globalization of Corporate Power, San Francisco: Earth Island Press.

Competencias: G1, G4, G7, G9, G20, G11 G13, G14, G18,G19 E1 Análisis de modelos del comercio internacional