

14.54 International Trade

— Lecture 1: Introduction —

Today's Plan

- 1 Course logistics
- 2 Why study international trade?
- 3 What is globalization?

1. Course Logistics

- **Required textbook:** Paul Krugman, Maurice Obstfeld, and Marc Melitz, International Economics, 9th edition, Addison-Wesley
- **Course requirements:**
 - Midterm exam (10/17): 35% of the course grade
 - Final exam (TBA): 50% of the course grade
 - Six problem sets: 15% of the course grade
- There is **no lecture** on Wednesday Nov. 23 (Thanksgiving)

1. Course Logistics

- **Course outline:**

- ① Basic facts (1 week)
- ② Comparative advantage and gains from trade (2.5 weeks)
- ③ Technology and trade (1 week)
- ④ Factor endowments and trade (3.5 weeks)
- ⑤ Increasing returns (1.5 week)
- ⑥ Trade policy (1.5 week)
- ⑦ International factor mobility (1.5 week)

2. Why Study International Trade?

Because national governments can—and do—restrict international movement of goods/services and factors of production

- International movements of production factors (immigration, foreign direct investment) are most severely restricted (relative to trade in goods and services)
 - ... with the most severe restrictions imposed on labor/immigration
 - Which forces are dominant is an empirical matter

2. Why Study International Trade?

Production technologies do not flow easily across borders

- There are massive differences in production technologies across countries (Not just tied to differences in the availability of physical factors of production)
- The use of some technologies is tied to human capital
 - ... which can not be transferred across countries
- Government institutions have a huge impact on the effectiveness of different technologies
 - Infrastructure for transport/communication
 - Legal system
 - Labor market institutions

2. Why Study International Trade?

In contrast, governments often protect and enable the free flow of goods and factors within borders

- Example of US constitution interstate commerce clause (section 8)
 - U.S. congress has the sole authority to regulate **all** forms of interstate commerce
 - Covers all movements of people, goods, and services across state lines
 - ... as well as communication and transportation between states
 - In effect, states are prohibited from interfering with any form of interstate commerce

So why is international trade so different than intra-national trade?

- Because factors of production and production technologies are most often specific to countries
- Countries have the ability to restrict trade

2. Why Study International Trade?

Because many politicians are opposed to trade...



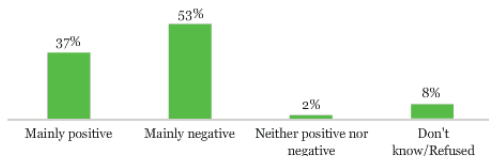
Courtesy of the White House. Image is in the public domain.

2. Why Study International Trade?

American voters are often opposed to trade...

American Views on NAFTA

Thinking about the North American Free Trade Agreement (or NAFTA) that includes Canada, the United States, and Mexico, what effect has NAFTA had on the U.S. economy? Has it been . . . ?



GALLUP POLL

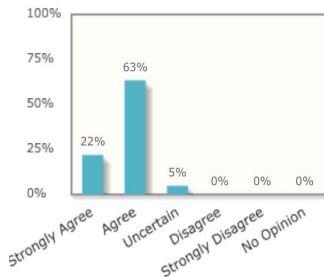
© Gallup, Inc. All rights reserved. This content is excluded from our Creative Commons license. For more information, see <https://ocw.mit.edu/help/faq-fair-use/>.

2. Why Study International Trade?

But economists, overwhelmingly, are not...

Question B: On average, citizens of the U.S. have been better off with the North American Free Trade Agreement than they would have been if the trade rules for the U.S., Canada and Mexico prior to NAFTA had remained in place.

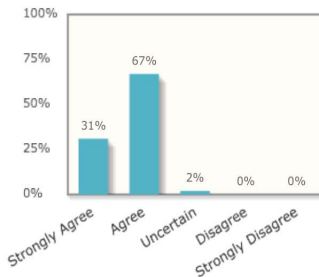
Responses



© 2016. Initiative on Global Markets.

Source: IGM Economic Experts Panel
www.igmchicago.org/igm-economic-experts-panel

Responses weighted by each expert's confidence



© 2016. Initiative on Global Markets.

Source: IGM Economic Experts Panel
www.igmchicago.org/igm-economic-experts-panel

© Chicago Booth. All rights reserved. This content is excluded from our Creative Commons license. For more information, see <https://ocw.mit.edu/help/faq-fair-use/>.

3. What is Globalization?

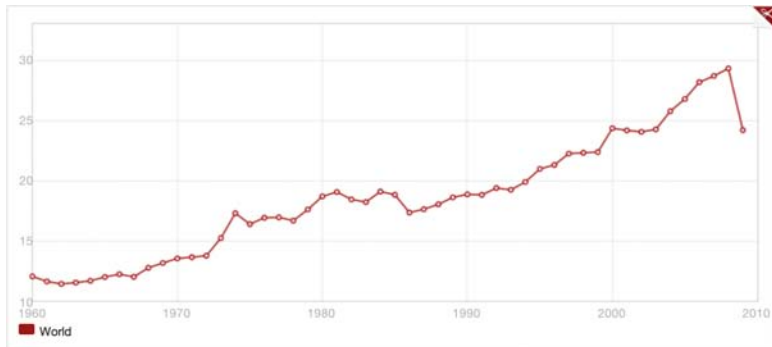
Definition from Deardorff and Stern Article:

- ① Increase in international transactions in markets for goods, services, and factors
- ② Growth and expanded scope of international institutions and organizations
 - Multinational Corporations
 - International Institutions: UN, World Bank, IMF, WTO

How Can Globalization Be Measured?

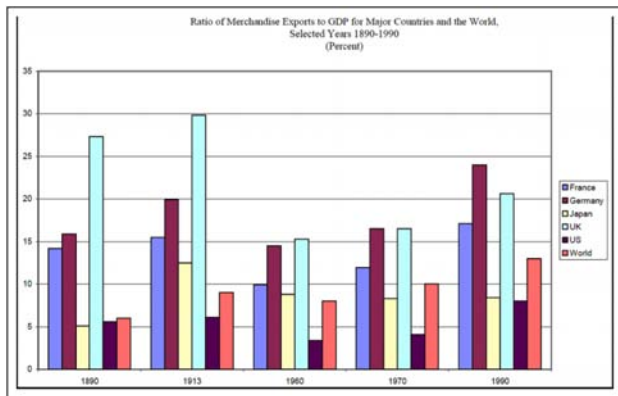
- **Trade flows:** exports and imports of goods
- **Trade in services:** transportation, healthcare, telecommunications, business services (consulting, IT, back-office, call center)...
- **Foreign asset ownership**
- **Immigration**
- **Price convergence:** Possibility of trade (even if it does not occur) may have important effects

Measure 1: World Exports Relative to World GDP



© Source unknown. All rights reserved. This content is excluded from our Creative Commons license. For more information, see <https://ocw.mit.edu/help/faq-fair-use/>.

Substantial Variation Across Countries in this Measure



Courtesy of Alan V. Deardorff and Robert M. Stern. Used with permission.

- U.S. and Japan are relatively closed economies (especially relative to other developed countries)
- Two waves of globalization: late 19th century and post WW2

Substantial Variation Across Countries in this Measure (Cont.)

Figure 1-2 from *International Economics* by Paul Krugman, Maurice Obstfeld, and Marc Melitz removed due to copyright restrictions.

Accounting for Regional Trade Groups

2005 in Million of US \$				
Region	Merchandise Exports			GDP
	Intra-Region	Rest of World	Total	
EU25	\$ 2,666,398 19.8%	\$ 1,345,872 10.0%	\$ 4,012,271 29.8%	\$ 13,443,077
EURO	\$ 1,567,451 15.8%	\$ 1,550,776 15.6%	\$ 3,118,227 31.3%	\$ 9,950,678
NAFTA	\$ 824,550 5.7%	\$ 653,425 4.5%	\$ 1,477,975 10.2%	\$ 14,442,879

© Source unknown. All rights reserved. This content is excluded from our Creative Commons license. For more information, see <https://ocw.mit.edu/help/faq-fair-use/>.

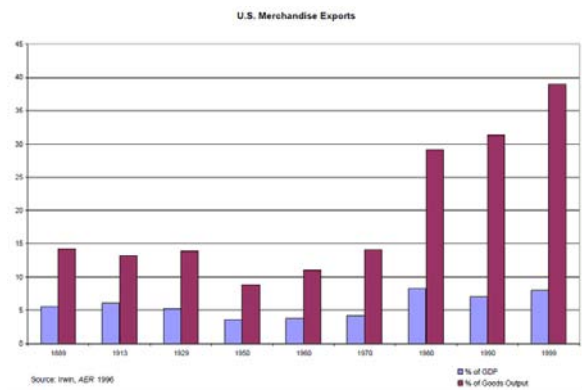
The U.S. Experience



© Source unknown. All rights reserved. This content is excluded from our Creative Commons license. For more information, see <https://ocw.mit.edu/help/faq-fair-use/>.

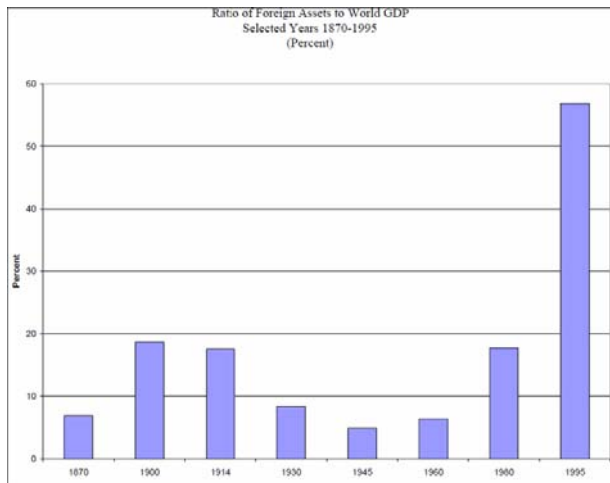
U.S. Exports and Manufacturing Output

- U.S. exports are a much more important part of total U.S. manufacturing:



As the U.S. economy has substantially concentrated into services

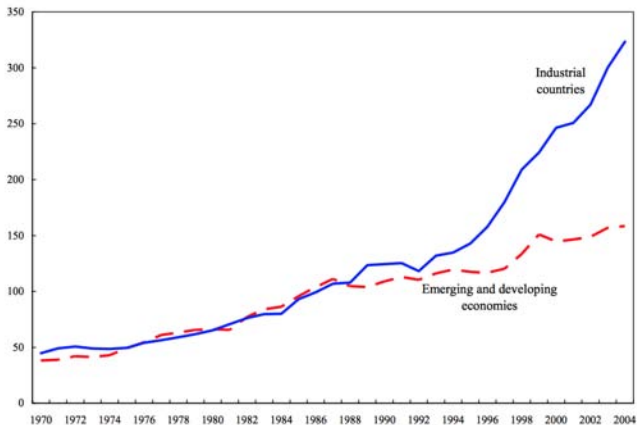
Measure 2: Foreign Asset Ownership



Courtesy of Alan V. Deardorff and Robert M. Stern. Used with permission.

Explosion in foreign asset ownership since 1990s

World Assets and Liabilities

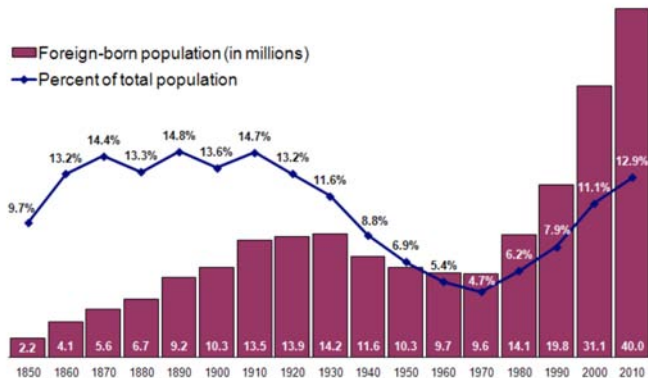


Note: Ratio of sum of foreign assets and liabilities to GDP, 1970-2004.

© International Monetary Fund. All rights reserved. This content is excluded from our Creative Commons license. For more information, see <https://ocw.mit.edu/help/faq-fair-use/>.

Measure 3: Immigration

Foreign-Born Population and Percentage of Total Population, for the United States: 1850 to 2010



Source: U.S. Census Bureau, Census of Population, 1850 to 2000, and the American Community Survey, 2010.



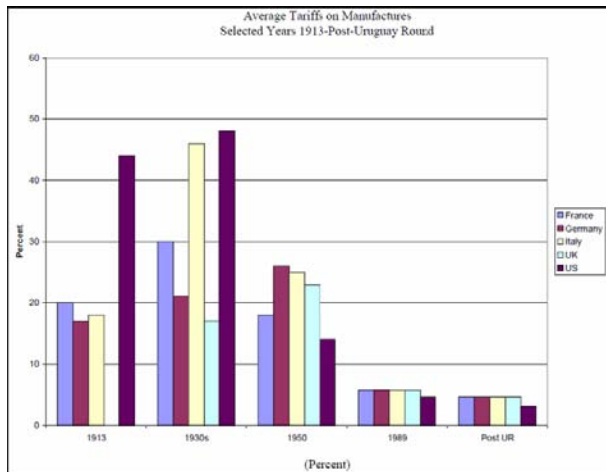
Courtesy of the United States Census Bureau. Image is in the public domain.

Measure 4: Price Convergence

- Fall in transportation costs in 19th century led to much greater price convergence than has been observed at any time since WW2
 - Example: Grain prices between Chicago and Liverpool
 - 60% difference in 1870 dropped to 15% in 1912
- Similarly, there was substantially more real wage convergence in the 19th century than since WW2

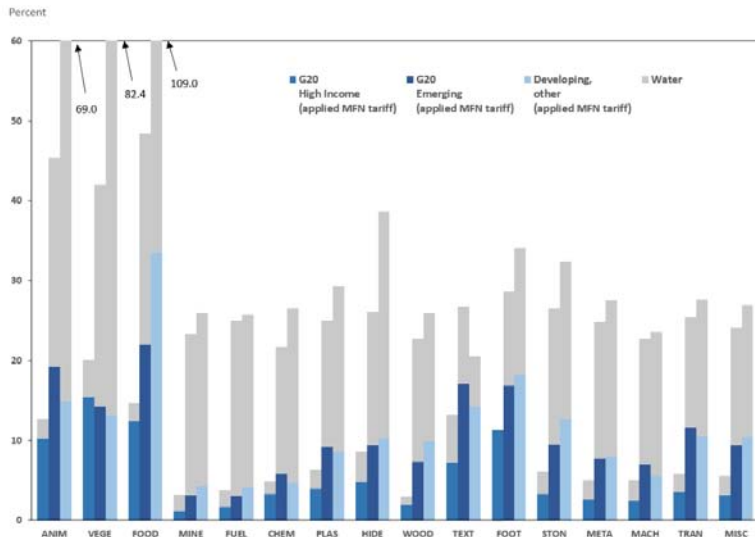
Causes of Globalization

- Drop in transport costs and communication costs
 - Telegraph vs. phone vs. internet
- Drop in tariffs: advent of GATT and then WTO



Courtesy of Alan V. Deardorff and Robert M. Stern. Used with permission.

Tariffs Across Countries and Industries in 2013



Courtesy of Elsevier, Inc., <http://www.sciencedirect.com>. Used with permission.

MIT OpenCourseWare
<https://ocw.mit.edu>

14.54 International Trade

Fall 2016

For information about citing these materials or our Terms of Use, visit: <https://ocw.mit.edu/terms>.