

Contents

1	Introduction	1
1.1	Overview	2
Part I International Trade Theory		
2	The Origins of International Trade Theory	7
2.1	Mercantilism	7
2.2	Absolute Advantage: Adam Smith	8
2.3	Comparative Advantage: David Ricardo	10
2.3.1	Opportunity Cost	11
2.4	Factors of Production: Labor and Capital	14
2.4.1	Factor Intensity	15
2.5	Ricardo's Simplifying Assumptions	15
	Simulated News Articles	16
	Article 2.1. Trade Minister Makes Controversial Speech	16
	Hints and Solutions	18
	Article 2.1	18
3	The Ricardian Trade Model	19
3.1	The Production Possibilities Frontier	20
3.2	The Production Possibilities Frontier with Increasing Costs	21
3.3	Indifference Curves	22
3.3.1	Consumer Preferences	23
3.3.2	Indifference Curves	24
3.4	Ricardo's Theory in Practice: The Ricardian Two-Step Trade Model	29
3.4.1	The Global Terms of Trade	30
3.5	Ricardo with Increasing Costs	37
3.5.1	Results	38
3.6	Benefits of Trade for Countries with the Same PPFs	39
3.7	Intra-Industry Trade	40

Articles	43
Article 3.1. Trade Pacts Spawns Conflict	43
Hints and Solutions	44
Article 3.1	44
4 Factor Intensity	47
4.1 Heckscher–Ohlin Theorem (HOT)	47
4.2 Stolper–Samuelson Theorem (SST)	50
4.3 The Six Steps to Increase the Overall Welfare of a Country	52
4.4 The Mundell Hypothesis	52
Articles	54
Article 4.1. Town Hall Tempest in Gettysburg	54
Hints and Solutions	56
Article 4.1	56
5 Stripping Away Ricardo’s Assumptions	57
5.1 Ricardian Assumption: Both Countries A and B Have Identical Technology	57
5.1.1 The Production Life Cycle (PLC)	58
5.2 Ricardian Assumption: Industries X and Y in Countries A and B Are Fully Competitive	61
5.2.1 Intra-Industry Trade	62
5.3 Ricardian Assumption: The Ricardian Model Only Has Two Countries, Two Goods, and Two Factors of Production	64
5.4 Ricardian Assumption: No International Factor Mobility: Resources Can Move Between Products X and Y Within Each Country but Cannot Move from One Country to Another	65
5.5 Ricardian Assumption: No Transportation, Environmental, or Infrastructure Costs	65
5.6 Ricardian Assumption: Full Employment of All Resources	66
Articles	67
Article 5.1. Trade Giants in Central New Jersey	67
Article 5.2. The Boeing 787 Dreamliner: A Global Affair	68
Hints and Solutions	70
Article 5.1	70
Article 5.2	72
6 Trade Barriers and Protectionism	75
6.1 Tariffs	76
6.1.1 Tariffs: 3 Types	76
6.1.2 Tariffs: How They Work	78
6.1.3 Tariffs: Prohibitive Tariff Eliminates Imports Entirely	80
6.1.4 Tariff Harms Domestic Consumers and Country Overall: General-Equilibrium Analysis	81

6.2	NTBs: Quotas and Hassle Factors	86
6.2.1	Quotas: Worse Than Tariffs	86
6.2.2	Tariffs and Quotas: Harmful Effects	88
6.3	Strategic Trade: Export Subsidies and CVDs	90
6.3.1	Strategic Trade: Why Export Subsidies Don't Work	93
6.3.2	Strategic Trade: Dumping	94
6.4	"Dumping" Is Rarely Straightforward in Practice and Is Difficult to Prove	96
6.4.1	Strategic Trade: Bringing a Dumping Case to the WTO	96
6.4.2	Strategic Trade: US Antidumping Regulations	97
6.5	Definitions: Outsourcing \neq Offshoring \neq Inshoring	98
6.5.1	Outsourcing	98
6.5.2	Offshoring	98
6.5.3	Inshoring	99
6.6	Immiserization	100
6.7	Samuelson's Savage Attack on Free Trade	102
6.7.1	Refuting Samuelson's Attack	104
	Articles	105
	Article 6.1. NanoRX: Is Ricardo Dead?	105
	Article 6.2. Trade Wars, Fine Wine, and Amazing Cheese	107
	Article 6.3. Dewey Lobbs Is the Anti-Ricardo	109
	Hints and Solutions	110
	Article 6.1	110
	Article 6.2	111
	Article 6.3	112

Part II Global Macroeconomics Policy Demystified

7	Global Macroeconomics	119
7.1	The National Savings Identity (NSI)	119
7.1.1	Output	120
7.1.2	Disposition of Output	121
7.2	The Fiscal and Current Account Balances in the NSI	122
7.2.1	The Fiscal Budget Deficit	123
7.2.2	Linking the Twin Deficits	124
7.3	Supply and Demand for Loanable Funds and Global Capital Markets	125
7.4	Two Hypothetical Examples of the NSI: The United States and China	129
7.4.1	USA	129
7.4.2	China	130
7.5	The Global Flow of Funds	131
	Articles	132
	Article 7.1. Tough Questions in Deficit Seminar	132
	Article 7.2. Panel Answers Tough Questions at Rutgers Symposium	133

Hints and Solutions	135
Article 7.1	135
Article 7.2	136
8 Exchange Rates	137
8.1 The Exchange Rate	137
8.2 Floating Exchange Rates	139
8.3 Spot, Forward, and Expected Exchange Rates	141
8.4 Pegged Exchange Rates	146
8.5 Managed Exchange Rates	149
8.6 Trade-Weighted Exchange Rate	150
8.7 Hot Capital Flows	151
8.7.1 Hot Capital: Uncovered Nominal Interest Arbitrage	152
8.7.2 Hot Capital: “The Carry Trade”	154
8.7.3 Hot Capital: Adjustment Toward Equilibrium	155
8.7.4 Iceland 2008: The Carry Trade Blows Up	156
Articles	162
Articles 8.1. The Yuan–Dollar Saga	162
Hints and Solutions	165
Article 8.1	165
9 The ISLM-BOP Model: The Goods Market, the Money Market, and the Balance of Payments	169
9.1 ISLM-BOP: The Engine Room	170
9.2 The Goods Market	171
9.2.1 C: Consumer Spending (Private Consumption)	171
9.2.2 I: Capital Investments	174
9.2.3 Contagion	177
9.2.4 G: Government Spending	177
9.2.5 Exp.: Exports (X)	177
9.2.6 Imp.: Imports (V)	178
9.2.7 The Trade Deficit ($X - V$)	179
9.2.8 The Output Function (“Y”)	179
9.3 The Money Market	180
9.3.1 Real Money Supply	181
9.3.2 Money Demand	181
9.3.3 The Money Market with Pegged Rates	182
9.3.4 Domestic Monetary Policy	183
9.4 The IS Function: Goods Market Equilibrium	185
9.4.1 Attitudes and Expectations: “ <u>A</u> ”	185
9.4.2 The IS Function	185
9.4.3 IS Exercises	186
9.4.4 Taxes and the IS Curve	188
9.5 The LM Function: Money Market Equilibrium	190
9.5.1 The LM Function	190
9.5.2 LM Exercises	191

9.5.3	Slope (k/h) of the LM Curve	193
9.5.4	IS–LM Equilibrium	194
9.6	The Balance of Payments (BOP)	195
9.6.1	Current Account Balance (CAB)	196
9.6.2	Capital Account Balance (KAB)	196
9.6.3	CAB, KAB, and the NSI	197
9.6.4	The Balance of Payments	198
9.6.5	BOP and the Foreign Exchange Markets	201
9.6.6	BOP Deficit ($BOP < 0$)	201
9.6.7	BOP Surplus ($BOP > 0$)	203
9.6.8	BOP Equation	203
9.6.9	BOP Under Perfectly Mobile Capital	205
9.6.10	Relationship Between Y , i , CAB, and KAB	206
9.6.11	BOP Exercises	207
9.7	General Equilibrium	209
9.8	Chart of Variables and Their Impact on IS, LM, BOP	210
9.9	Survival Guide to ISLM-BOP Policy Analysis	212
9.10	Exercises with the ISLM-BOP Model	213
9.11	ISLM-BOP Survival Guide: Recap	221
	Articles	222
	Article 9.1. Hibernia Wrestles with Policy Options	222
	Hints and Solutions	223
	Article 9.1	223
10	Exports and Imports, Real Exchange Rates	229
10.1	Exports and Imports: Global Overview	229
10.2	Exports and Imports and the ISLM-BOP	234
10.3	Real Exchange Rates	238
10.4	The Pass-Through Effect	239
10.5	The Plaza Accord	240
10.6	Real Exchange Rate Parity: Relative PPP	243
10.7	General Parity Relationships: Expected Exchange Rates, Inflation, and Interest Rates	244
10.8	Purchasing Power Parity and Nominal GDP Comparisons	245
	Articles	246
	Article 10.1. Three Recent Articles from the <i>Lykos Free Press</i>	246
	Hints and Solutions	248
	Article 10.1	248
11	Incorporating Inflation into the Model	253
11.1	Inflation in the ISLM-BOP Analysis	254
11.2	The Benefits of Monetary Discipline	257

11.3	Speculative Asset Price Bubbles	258
11.3.1	“The Great Moderation”	262
11.3.2	Summary: “The Great Moderation” and Its Aftermath	269
11.4	Exploding Pegs	270
11.5	The Impossible Trinity	273
11.5.1	Fixed Exchange Rate and Perfectly Mobile Capital: Cannot Control Interest Rates	273
11.5.2	Fixed Exchange Rate and Control Over Monetary Policy: Cannot Permit Capital Mobility	274
11.5.3	Discretionary Monetary Policy and Perfect Capital Mobility: Cannot Maintain an Exchange-Rate Peg	275
11.5.4	Perfect Capital Mobility, Pegged Exchange Rates, and Discretionary Monetary Policy: Welcome to the Impossible Trinity	275
11.6	Southeast Asia 1997: The Good Times, the Bad Times, and the Brilliance of Dr. Hu	276
11.6.1	The Good Times	276
11.6.2	The Bad Times	277
11.7	Southeast Asia 1996–1997	279
11.7.1	Selected Southeast Asian Exchange Rates 1992–2000 ..	281
11.7.2	The Brilliance of Dr. Hu	281
	Articles	286
	Article 11.1. Puddingstones, Agate, and Global Macropolicy	286
	Hints and Solutions	288
	Article 11.1	288
12	Capital Flows: Perfectly and Imperfectly Mobile Capital	291
12.1	ISLM-BOP with Imperfectly Mobile Capital	291
12.2	The Keynesian Multiplier in Action	295
12.3	The Dornbusch Model of Sustainability	301
12.3.1	Fiscal Deficit Sustainability	301
12.3.2	Rudiger Dornbusch	301
12.3.3	The Dornbusch Model of Fiscal Deficit Sustainability	302
12.4	The European Economic and Monetary Union and the Euro	306
12.4.1	1946 Churchill: “United States of Europe”	306
12.4.2	1957 Treaty of Rome	307
12.4.3	1979 European Economic and Monetary Union	307
12.4.4	1985 White Paper	308
12.4.5	1986 Single European Act	309
12.4.6	1979–1991 Era of the ECU	310

12.4.7	End of the ECU	310
12.4.8	1999 The Euro	316
12.4.9	2010–? European Sovereign Debt Crisis	317
12.4.10	The Future of the Euro	321
12.5	Speculative Attacks and Overshooting	322
12.5.1	Speculative Attacks	322
12.5.2	Overshooting	325
12.6	Bigger Than Central Banks? Global Investors and the Balance of Financial Power	329
12.6.1	Size	330
12.6.2	FX Intervention	333
12.6.3	Monetary Policy	333
12.6.4	The Limits of Active Policy in an Open Economy	336
12.6.5	The Source of a Central Bank's Power	336
12.6.6	The Straw That Breaks the Camel's Back	338
Articles	339
	Article 12.1. The Sarangam Economy: A Retrospective	339
Hints and Solutions	340
	Article 12.1	340
13	The Global Monetary System	343
13.1	Foreign Exchange Sterilization	344
13.2	The Chinese Yuan	348
13.2.1	So, Who is Responsible for the US–China Trade and Currency Imbalance?	358
13.2.2	Something for Nothing: IP Theft, Economic and Industrial Espionage, and Technology Bleed	363
13.3	Global Imbalances and the “Savings Glut”	366
13.4	The US Dollar's Role as the World's Reserve Currency: Past, Present, and Future	368
13.4.1	History	370
13.4.2	Reserve Currencies over Time	371
13.4.3	The Future of the US Dollar as the World's Reserve Currency	373
13.4.4	The Chinese Yuan	375
13.4.5	The Japanese Yen	376
13.4.6	Developing and Growing Economies: India, Brazil, and South Korea	377
13.4.7	SDRs	377
13.4.8	The Euro	378
13.4.9	The US Dollar's Future	378
13.5	The Gold Standard	382
13.5.1	Money	382
13.5.2	Paper Money Backed by Precious Metal	384

13.5.3	The Gold Standard	385
13.5.4	The Gold-Dollar Standard	390
13.5.5	Fiat Paper Currency	391
13.6	A Return to the Gold Standard?	392
References		395
Index		401

International Trade and Global Macropolicy

Langdana, F.; Murphy, P.T.

2014, XVIII, 405 p. 261 illus., 215 illus. in color.,

Hardcover

ISBN: 978-1-4614-1634-0