

The University of Illinois at Chicago
Economics 514: International Trade Theory and Policy
Spring 1999

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Office Hours:

Mon.11 & Thurs.1,
and by appointment

Required Texts:

J. Markusen, J. Melvin, W. Kaempfer, and K. Maskus: *International Trade: Theory and Evidence*, McGraw Hill 1995. (MMKM)

J. Baghwati: *International Trade: Selected Readings*, MIT Press, 1987. (A collection of journal articles in international trade theory) (B)

W. Ethier, E. Helpman, and J.P. Neary: *Theory, Policy and Dynamics in International Trade*, Cambridge University Press 1993. (EHN)

Other Recommended Texts:

R. E. Caves, J. A. Frankel, and R. W. Jones: *World Trade and Payments: An Introduction*, 7th Edition, HarperCollins 1996. (A good undergraduate/graduate text with math explained in appendices)

A. Dixit and V. Norman: *Theory of International Trade*, Cambridge University Press, 1980. (A widely-used text, but has been out of print)

P. Krugman and M. Obstfeld: *International Economics: Theory and Policy*, Addison Wesley 1997. (A comprehensive text with good coverage of the recent research in the effects of increasing returns and product differentiation on trade and welfare.)

K. Wong: *International Trade in Goods and Factor Mobility*, MIT Press, 1995. (Advanced theory)

Classics:

Baghwati, "The Pure Theory of International Trade: A Survey," *Economic Journal*, 1964.

Caves and Johnson, eds., *AEA Readings in International Economics*, Irwin.

Chipman, "A Survey of the Theory of International Trade," 3 survey articles in *Econometrica*, June 1965, October 1965, and February 1966.

Kemp, *The Pure Theory of International Trade and Investment*, Prentice-Hall.

Meade, *A Geometry of International Trade*, Allen and Unwin.

Takayama, *International Trade*, Holt, Rinehart, and Winston.

Overview:

This is the first course in the graduate sequence in International Economics. Its purpose is to provide a broad survey of International Trade Theory and Trade Policy. Part I gives a quick introduction to the basic data and patterns of international trade. Part II introduces the basic trade model, how trade affects prices, wages, and consumption, and examines who gets the gains from trade.

Part III expands the basic trade model to study patterns of wage differences, nontraded goods, and empirical trade patterns. Part IV introduces trade policy, tariffs and other protection, managed trade, and regional trade agreements. Part V examines the integration of goods markets and financial markets in the balance of payments accounts.

Evaluation:

Credit for the course will be based on class participation and at least 2 practice problem sets (10%), class presentation (15%), the Mid-Term Examination (30%), and the Final Examination (45%).

Course Outline:**I. INTRODUCTION**

1. Current Issues and Patterns of International Trade in Goods and Services (MMKM: Chapter 1. See also *1996 Economic Report of the President*, Chapter 8, "The United States in the World Economy")

II. THE BASIC TRADE MODEL

2. 2 Countries, 2 Goods, 2 (Nontraded) Inputs (MMKM: Chapter 2, B: Chapter 3)
Recommended Reading: R. Jones, "The Structure of Simple General Equilibrium Models," *Journal of Political Economy*, December 1965. Also, Melvin, "Production and Trade with 2 Factors and 3 Goods," *American Economic Review*, December 1968.
3. Comparative Advantage and Production: Moving from Autarky or Shocks to Equilibrium (MMKM: Chapters 3, 4 and 5, and B: Chapter 4.) Recommended Reading: P: J. D. Richardson, "Income Inequality and Trade: How to Think, What to Conclude," *Journal of Economic Perspectives*, 9 (3), pp. 33-55.) Corden, "The Normative Theory of International Trade," in Jones and Kenen, Chapter 2, parts 1 and 2. Also, J. Bhagwati, "Immiserizing Growth: A Geometrical Note," *Review of Economic Studies*, 25 (3), June 1958, pp. 201-205.
4. Technology and Trade: The Ricardian Model of 2 Goods, 1 Factor (MMKM: Chapters 6-7)
Recommended Reading: R. Dornbusch, S. Fischer, and P. Samuelson, "Comparative Advantage, Trade and Payments in a Ricardian Model with a Continuum of Goods," *American Economic Review*, 67, December 1977, pp. 823-839. Also, Markusen and Svensson, "Trade in Goods and Factors with International Differences in Production Technology," *International Economic Review*, 1985.

5. Results of Classic Trade Theory using the Heckscher-Ohlin 2X2 Model (MMKM: Chapter 8 and B: Chapters 1, 8) Recommended Reading: P. Samuelson, "International Trade and the Equalisation of Factor Prices," *Economic Journal* 58, 1948, pp. 163-184. Also, Stolper and Samuelson, "Protection and Real Wages," *Review of Economic Studies*, 1941. Rybczynski, "Factor Proportions and the Heckscher-Ohlin Theorem," *Economica*, 1955. Helpman, "The Factor content of Foreign Trade," *Economic Journal*, 1984. Treffler, "International Factor Price Differences: Leontief was Right!" *Journal of Political Economy*, December 1993.
6. Specific Factors and Nontraded Goods (MMKM: Chapter 9 and B: Chapter 5) Recommended Reading: M. Mussa, "Tariffs and the Distribution of Income: The importance of Factor Specificity, Substitutability, and Intensity in the Short and Long Run," *Journal of Political Economy* 82 (1974) pp. 1191-1204.

III. TRADE POLICY

7. Tariffs (MMKM: Chapter 10, B: Chapter 13, and JHN: Chapter 9) Recommended Reading: V. Corbo, "Trade Reform and Uniform Import Tariffs: The Chilean Experience," *The American Economic Review* 87 (2), pp. 73-77.) Corden, "The Structure of a Tariff System and the Effective Protective Rate," *Journal of Political Economy*, 1966.
8. Comparing Protection Policies: Tariffs, Quotas, Subsidies and Managed Trade (MMKM Chapters 15-16, B: Chapter 14, and JHN Chapter 10) Recommended Reading: Jones, "Effective Protection and Substitution," *Journal of International Economics*, 1971. Also, Dixit, "How Should the U.S. Respond to Other Countries' Trade Policies?" in Stern, ed., *U.S. Trade Policies in a Changing World Economy*, MIT 1987.
9. Regional Trade Agreements, and other new developments (MMKM: Chapter 18-20 and B: Chapters 20-21) Recommended Readings: P: J. Bhagwati and A. Panagariya, "Regionalism versus Multilateralism: The Theory of Preferential Trade Agreements: Historical Evolution and Current Trends", *The American Economic Review* 86 (2) pp. 82-98.)

IV. EFFECTS OF INCREASING RETURNS AND MARKET STRUCTURE

10. Economies of Scale and Imperfect Competition (MMKM: Chapter 11-12, B: Chapter 9) Recommended Reading: E. Helpman and P. Krugman, *Market Structure and Foreign Trade*, 1985, MIT Press., especially Chapters 4-9 and Ethier, "Internationally Decreasing Costs and World Trade," *Journal of International Economics*, February, 1979. Also, Markusen, "Trade in Producer Services and in Other Specialized Intermediate Inputs," *American Economic Review*, March 1989 and Balassa, "Intra-Industry Specialization: A Cross-country Analysis," *European Economic Review*,

1986.

11. Imperfect Competition and Trade Policy (MMKM: Chapter 17 and B: Chapter 12)
Recommended Readings: Markusen and Venables, "Trade Policy with Increasing Returns and Imperfect Competition: Contradictory Results from Competing Assumptions," Chapter 8 in Grossman, ed., *Imperfect Competition and International Trade*, MIT Press.

V. TRADE, GROWTH AND DYNAMICS

12. Factor Trade and Direct Foreign Investment (MMKM: Chapters 21-22, B: Chapters 22, 24, 25)
13. Hysteresis (MMKM: Chapter 23 and EHN: Chapters 8, 16)
14. Stochastic Economy (JHN: Chapters 11-14)

VI. BALANCE OF PAYMENTS ACCOUNTS

15. Current and Capital Accounts (B: Chapter 2) Recommended Readings: Caves, Frankel and Jones: Chapter 16 and R. McKinnon and H. Pill, "Credible Economic Liberalizations and Overborrowing," *The American Economic Review*, 87 (2) pp. 189-193. Markusen, "Factor Movements and Commodity Trade as Complements," *Journal of International Economics*, 1983, Svensson, "Factor Trade and Goods Trade," *Journal of international Economics*, 1985.