Lecture #1
Economics 181
International Trade
Introduction

1. Course Contents

What do you think you will study in this course?

What will we actually study in this course? (Review course outline)

2. Defining international trade:

International trade studies the issues related to the exchange of goods, services and factors or production between traders across distinct (national) markets.

Main goal of this course: To provide you with tools to think about the issues related to international trade and to analyze trade policy.

Why is international trade different from other economics?

It is often said that the extent of present day globalization (usually defined as the integration of world markets for goods, services and capital) is unsurpassed. We now examine features of current day globalization. Is more integration likely or possible?

3. Some Broad Trends in International Trade

1.1 How have trade flows increased?

How does the US look relative to other countries?

1.2 Why have trade flows increased so much?
How did protection compare in the US versus other countries in the past?
How does it compare today?

3.3 How has the composition of trade changed?

4.4 How have other measures of globalization changed? Enormous increases in direct foreign investment (DFI).

2. Introducing the Ricardian model of Trade.

4.1 We begin with a puzzle.

In 1998, the following man-hours were required to produce a ton of steel in the US and elsewhere:

USA	
Old integrated steel mills	5 man-hours to produce 1 ton of steel
New mini-mills	.5 man-hours to produce 1 ton of steel
Japan	6 man-hours to produce 1 ton of steel
Russia	8 man-hours to produce 1 ton of steel.

Which country is the most efficient?
Does the US import or export steel? Why?

4.2 Benefits of the framework

The Ricardian model is a framework for explaining why countries trade, and it also helps to explain the pattern of trade. It is also a useful framework for understanding why it is not possible to set equal wages all over the world—or to set the same minimum wage in Mexico and the United States, for example.

Three Useful Insights:

- We can explain why all countries gain from trade.
- We can determine the pattern of trade—ie what the US, Germany, or any other country is likely to export.
- The framework helps us to understand where income differences come from

Key Assumptions

- One factor of production:labor
- Technology varies across countries
- Constant returns to scale
- Perfect Competition

4.3 Gains from Trade

Example #1	Roses		Computers
USA	10 million	OR	100,000
Colombia	10 million	OR	30,000

Opportunity cost: The opportunity cost of roses in terms of computers is the number of computers that could have been produced with the resources used to produce a given number of roses.

Gains from trade: can re-arrange production so that with the same amount of resources, get more output:

	Roses	Computers
USA	-10 million	+100,000
Colombia	+10 million	-30,000
Total	0	+70,000

Example #2
Two countries: Home (USA) and Foreign (France). Two goods: wine and cheese.
Unit labor requirements (ULR): number of labor hours needed to produce one unit of wine or Cheese

Hours to Produce 1 pound of Cheese or 1 gallon of wine

	Cheese	Wine	Total Labor Force (Billion Hours)
Home (USA)	$a_c = 1$	$a_w = 2$	120
Foreign (France)	$a_c^* = 6$	$a_w^* = 3$	60

Can re-arrange production so that there are gains from trade:

	Wine	Cheese
USA	-1	+2
France	+1	-1/2
Total	0	+1 and 1/2