

International Trade and Monetary Systems

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Syllabus

Week	Topic	Reading Assignment
1	Introduction to International Trade	Ch. 1
2	The Heterodox Approach	Ch. 2
3	International Trade Theory	Ch. 3
4	International Trade: Beyond the Neoclassical Perspective	Ch. 4
5	Imperfect Competition & Transnational Corporations	Ch. 5
6	International Trade & Economic Development	Ch. 6
7	International Trade, Human Happiness, and Unequal Economic Development	Ch. 7
8	Tariffs, Quotas, & Trade Restrictions	Ch. 8
9	History of Trade Policy	Ch. 9
10	International Trade Policy: A Holistic Perspective	Ch. 10
11	Early Monetary History	Ch. 15
12	The International Monetary System	Ch. 16
13	Do we need a new Bretton Woods Conference?	Ch. 17
14	Review	
15	Final	

Mandatory Readings

- ▶ Hendrik Van den Berg, *International Economics: A Heterodox Approach* (2nd edition), 2012, Routledge.

Grading

- 33% Class Participation
- 33% Quizzes and Homeworks
- 33% Final Exam

Interdependence

There are three fundamental advantages from expanding the number of people in a society:

1. The gain from specialization
 - ▶ Comparative advantage
 - ▶ Economies of scale
2. The potential for risk reduction
3. The creation of knowledge

These three advantages are mutually reinforcing!
Interdependence!

Interaction with strangers has many dangers

- ▶ The survival of the human species and the maximization of individual welfare has always required a careful **balance between interaction and isolation**.
- ▶ The recent improvements in human welfare, longevity, and quality of life are the result of our improved ability to reduce the propensity for humans to exploit, steal, and kill.
- ▶ It seems to have become easier and safer to deal with strangers.

Institutions

- ▶ In order to capture the gains from
 - ▶ specialization,
 - ▶ risk sharing, and
 - ▶ knowledge creation,we must create institutions that make human beings, who are hard-wired to be suspicious of strangers, willing to deal with strangers [Douglass North].
- ▶ R..almost all of the institutions of modern society can be understood as dedicated to an utterly unnatural division of labor between strangers.S
- ▶ Humans have struggled to get the institutions right.

Institutions

- ▶ If the objectives of those players in a position to shape their destiny are met, it is possible to say that society has created a consistent set of institutions.
- ▶ Rmprovement has been a trial and error process of change with lots of errors, endless losers, and no guarantee that we will continue to get it right in spite of the enormous accretion of knowledge over those centuries.S

Individuals vs Society

Douglass North suggests that the frequent inconsistencies between people's objectives and society's actual outcomes are caused by:

- ▶ The lack of accurate information on how the world actually is and how it functions.
- ▶ The resistance to change by certain people and groups of people because they prefer the status quo to further change.
- ▶ The acceleration of economic growth over the past several centuries suggests that we have been Rgetting it rightS more often.

Many problems remain

- ▶ The di] erences in the rates of change of
 - ▶ reality,
 - ▶ knowledge,
 - ▶ formal legal institutions,
 - ▶ culture, and
 - ▶ human instinctmean that when economic and social environments change more rapidly, humans' culture and evolutionary hard-wired behavioral systems often fall behind.
- ▶ Historical evidence shows episodes of expanding international economic integration are often reversed because institutional support is not su, cient to handle the complex international economic interactions.

Institutions

- ▶ Institutions are both formal and informal arrangements and guidelines.
- ▶ Culture is an informal institution.
- ▶ Culture includes
 - ▶ the stories,
 - ▶ myths,
 - ▶ religions,
 - ▶ traditions,
 - ▶ rituals, and
 - ▶ widely accepted beliefsthat give meaning to our social existence.
- ▶ Culture changes slowly.
- ▶ Culture may clash with reality and other cultures.

International Trade & Institutions

- ▶ International economic activity is greatly hampered by di] erences in institutions across countries.
- ▶ International trade, international investment, international financial transactions, and international migration involve complex forms of human interaction.
- ▶ When cultures, rules, laws, and traditions di] er, people have trouble carrying out international trade, international investment, long-term lending and borrowing, and absorbing foreign immigrants.
- ▶ The important lesson here is that human interactions with strangers have not, and still do not, always turn out to be mutually beneficial for all involved.

International Trade in Context

International economics has, traditionally, focused on four different components of international economic integration:

- ▶ International trade
- ▶ International investment
- ▶ International finance
- ▶ International migration

International Trade in Context

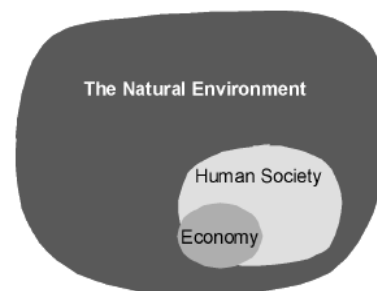
The four components of international economic integration are related:

- ▶ Trade often involves financing.
 - ▶ Investment implicitly always involves financing.
 - ▶ Migration is often related to investment.
 - ▶ Investment is related to trade.
- ▶ We focus on one of these components, but the international economy is a complex system in which all components are tightly linked in a great variety of ways.

Mainstream, Orthodox

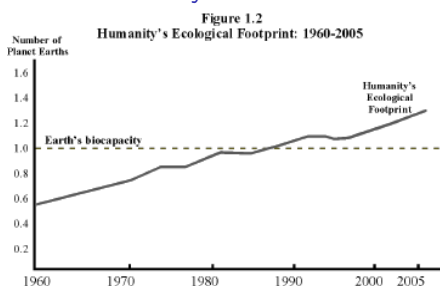
- ▶ Beginning with **Adam Smith** and **David Ricardo**, economists have developed economic models that support the hypothesis of a **positive relationship between international economic integration and human well being**.
- ▶ Textbooks in international economics frame their analysis around these models, which we will refer to as mainstream, or orthodox, international economics.
- ▶ Many people remain **unconvinced** by economists' theoretical arguments, however.
- ▶ The large gap between most economists' active advocacy of policies to promote international economic integration and the general public's distrust is driven by general perceptions of how international economic integration affects human society.

Variety of perspectives, a heterodox approach



- ▶ In this course, we first place the economy within human society, which we then link to the earth's ecosystem and the universe beyond.
- ▶ The economic sphere is linked to the social sphere in many complex ways, and human society, in turn, interacts with the natural sphere, in many complex ways.

Ecological Sustainability



- ▶ Earth's ecosystem is under severe pressure from the past and present growth of the human population and their expanding environmental footprint.
- ▶ In the 1980s, humanity began using Earth's services at a rate that exceeded the capacity of the ecosystem to replenish itself.

Green Revolution

- ▶ Humanity's efforts to compensate for the stress on nature's renewable services as well as the depletion of non-renewable resources have often made things worse.
- ▶ The so-called Green Revolution that increased the amount of food produced per acre during the latter half of the twentieth century has caused numerous stresses in the social and natural spheres.
- ▶ The consequences show up in the form of growing urban slums, mass illegal immigration, broken family structures, and greater income inequality.
- ▶ Modern agriculture, among all sectors of the economy, is the single largest contributor to global warming, even larger than transportation and power generation.

Social Conflicts

- ▶ Growth and international integration of economic activity has also caused severe social conflicts and oppression.
- ▶ The growing demand for material output has in recent years triggered wars over oil supplies in Kuwait, Iraq, and Georgia, and repeated threats of war by petroleum importers such as the US against oil producers like Iran, Venezuela, and Ecuador.
- ▶ Civil wars in more than a dozen African countries are really fights over control of natural resources.
- ▶ Large countries such as China, the US, Russia, and others are actively engaged in a military arms race in order to expand and maintain their control over the world's scarce resources.
- ▶ Countries have developed or are seeking to develop nuclear weapons to protect themselves and their resources.

Globalization

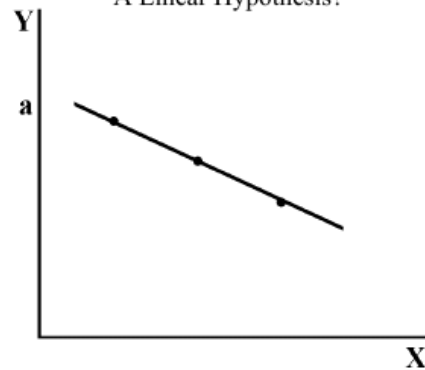
- ▶ International economic integration has disrupted traditional societies and their customary economic relationships.
- ▶ Globalization's social stresses manifest themselves in many ways:
 - ▶ The long-distance international migration of millions of people.
 - ▶ Rising income inequalities within most of the world's countries.
 - ▶ Hunger for one billion of the world's seven billion people despite enough global agricultural production to feed nine billion people.
 - ▶ High unemployment even in rapidly-growing economies.

Model Complexity

- ▶ The overwhelming complexity of our world means that social scientists must develop hypotheses that are simplified representations of that complexity.
- ▶ In economics, we refer to such simple hypotheses as models.
- ▶ We will often describe and use models in this textbook because many of them do help us understand the process of international economic integration.
- ▶ It is useful, therefore, to review what models are, why we use them, and how they help us understand complex phenomena.

Graphic example of a model that relates 2 variables

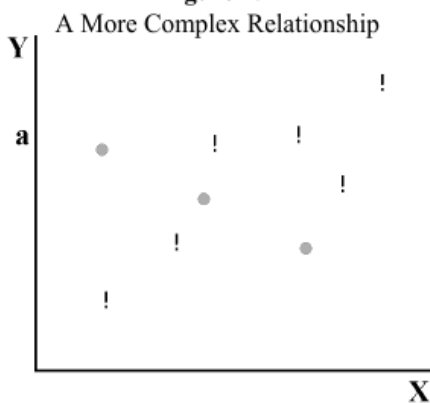
Figure 1.3
A Linear Hypothesis?



Graphic example of a model that relates 2 variables

But, what if further analysis reveals more data points? What is the most likely relationship now?

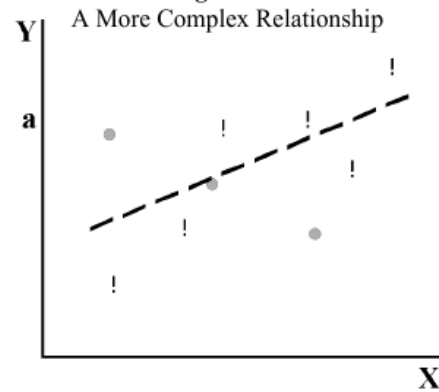
Figure 1.4



Graphic example of a model that relates 2 variables

Is the line below a more accurate description of the relationship between X and Y?

Figure 1.4



Critically question the model

- ▶ These examples suggest that economic models based on a small number of observations should not be taken uncritically as definitive proof for or against a hypothesis.
- ▶ A **holistic** perspective on the matter would suggest that, because the scatter of points do not lie on a simple straight line, the relationship between international trade and per capita GDP depends on other influences.
- ▶ Perhaps we have not specified our model correctly. Perhaps the equation is not linear.
- ▶ Perhaps we do not understand what are the causal variables, and what are the caused variables.

Oversimplification?

- ▶ More sophisticated statistical regression models, which simultaneously account for the influence of many variables and, effectively, look at more dimensions than the simple relationships shown in the Figures, can be used to uncover other variables that affect how exports translate into GDP per capita.
- ▶ **Heterodox** economists are, therefore, quite skeptical of most statistical results.
- ▶ They understand that there are no simple relationships where only one variable, X, entirely determines the value of another variable Y.

Assumptions may determine conclusions

- ▶ The particular set of models that economists use determines their perspective they take on the subjects they seek to understand and analyze.
- ▶ Students are misled by most textbooks to believe that there is just one paradigm in (the field of international) economics, namely the neoclassical paradigm, and that models that fit the neoclassical paradigm, neoclassical models in other words, can be used to analyze all economic issues.
- ▶ There are actually many paradigms in economics.
- ▶ Conclusions about international trade, investment, finance, and migration differ substantially depending on which paradigm is used.

Neoclassical Paradigm & Free Trade

- ▶ (International) economists most often embrace the neoclassical paradigm.
- ▶ Models based on the neoclassical assumptions inevitably predict that free trade, unrestricted international investment, unregulated international finance, and unrestricted immigration are welfare maximizing.
- ▶ (International) economists seem to have become reluctant to extend the models and focus on broader issues, perhaps for fear of undermining the pro-international economic integration culture of the field.
- ▶ (The field of international) economics has created a culture that takes the neoclassical models conclusions as truth.

A Variety of Perspectives

- ▶ We take a heterodox approach to international economics.
- ▶ We cover most of the same topics and issues covered in mainstream international economics courses, but we will use a variety of models from many different paradigms.
- ▶ Heterodox economists use models, too, but unlike mainstream economists, heterodox economists resist relying on just one model or one set of related models generated under one uniform set of assumptions.
- ▶ Next week we discuss the heterodox approach in more detail.