



Osher Lifelong Learning Institute, Fall 2023

Contemporary Economic Policy

American University
Fall, 2023

Jon Haveman, Ph.D.
National Economic Education Delegation



Course Outline

- **Contemporary Economic Policy**

- Week 1 (9/28): US Federal Budget (Jon Haveman, NEED)
- **Week 2 (10/5): Trade and Globalization (Arkadiusz Mironko, Indiana Univ. East)**
- Week 3 (10/12): International Institutions (Alan Deardorff U of Michigan)
- Week 4 (10/19): Economic Update (Geoffrey Woglom Amherst College)
- Week 5 (10/26): Monetary Policy (Geoffrey Woglom)
- Week 6 (11/02): Intro to Financial Economics (Geoffrey Woglom)

Submitting Questions

- **Please submit questions in the chat.**
 - I will try to handle them as they come up, but may take them in a bunch as time permits.
- **We will do a verbal Q&A once the material has been presented.**
 - And the questions in the chat have been addressed.
- **OLLI allowing, we can stay beyond the end of class to have further discussion.**

Credits and Disclaimer

- **This slide deck was authored by:**
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 - James Lake, Southern Methodist University
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 - Alan Deardorff, University of Michigan
 - Ed Leamer, UCLA
- **Disclaimer**
 - NEED presentations are designed to be nonpartisan.
 - It is, however, inevitable that the presenter will be asked for and will provide their own views.
 - Such views are those of the presenter and not necessarily those of the National Economic Education Delegation (NEED).

Outline

- What is Globalization?
- Pros and Cons of Trade
- Trade Policies
- The Role of Trade Agreements
- (Effects of the Pandemic and War)

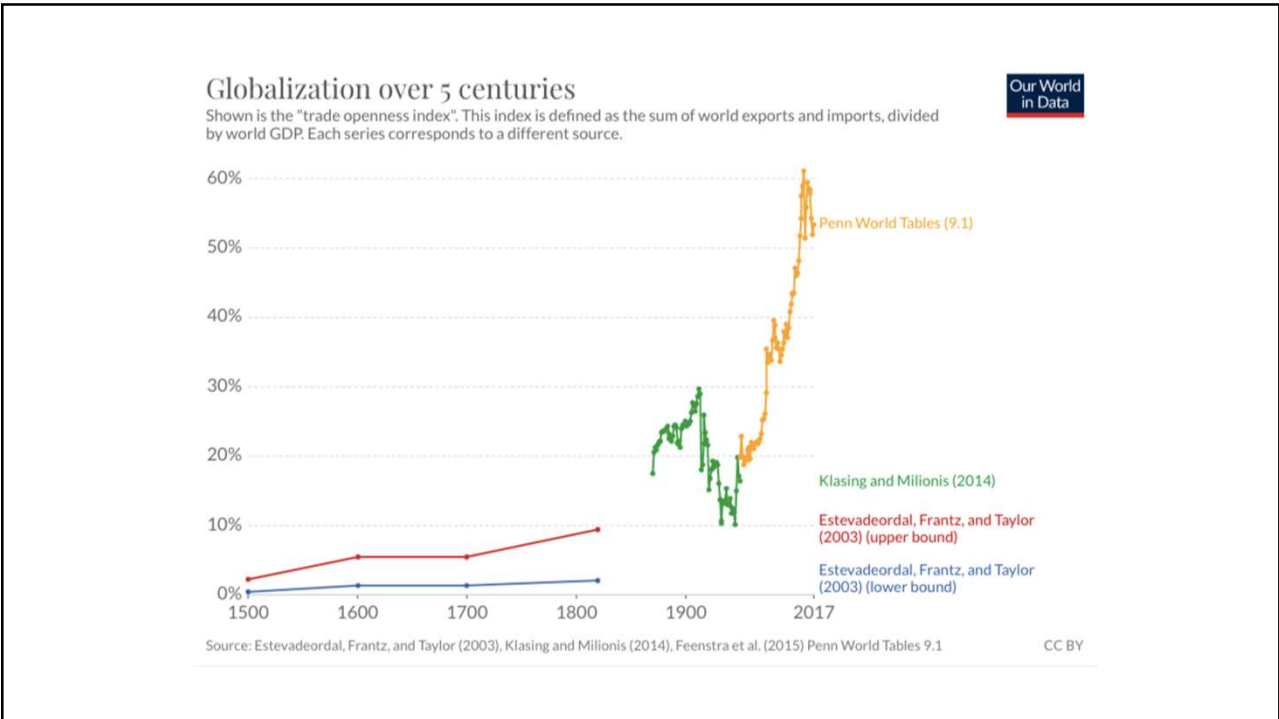
What Globalization is

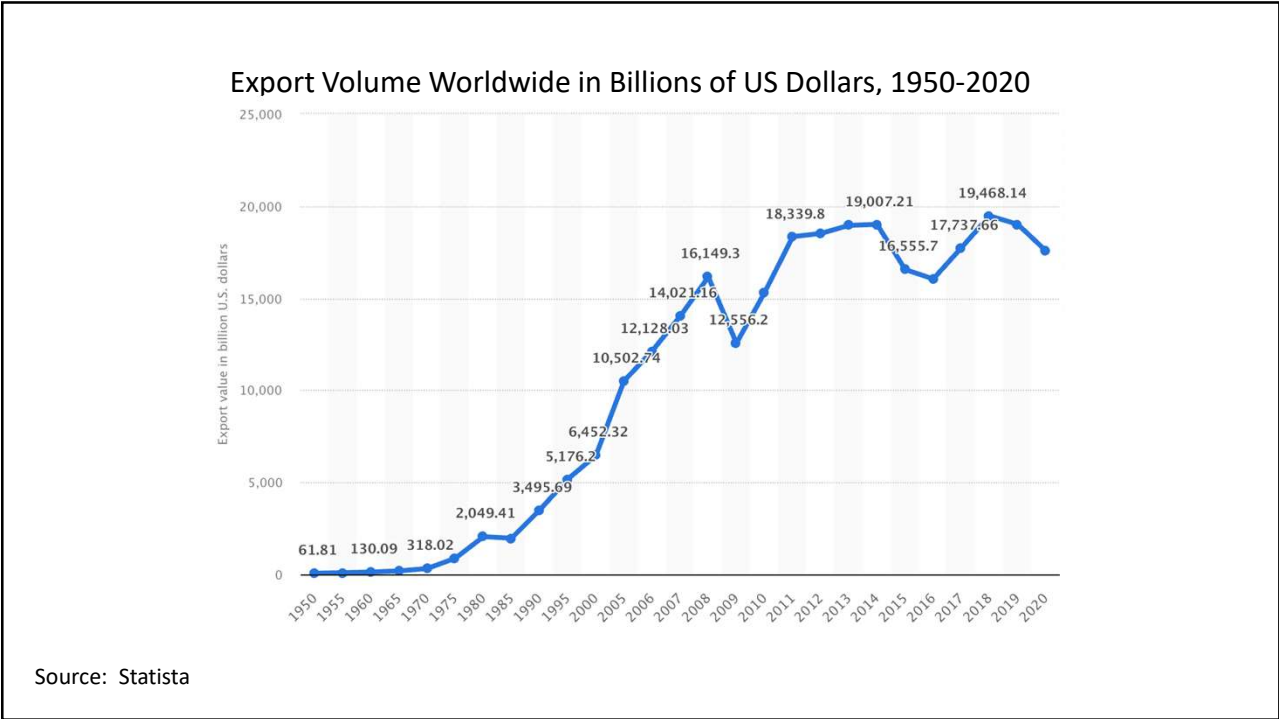
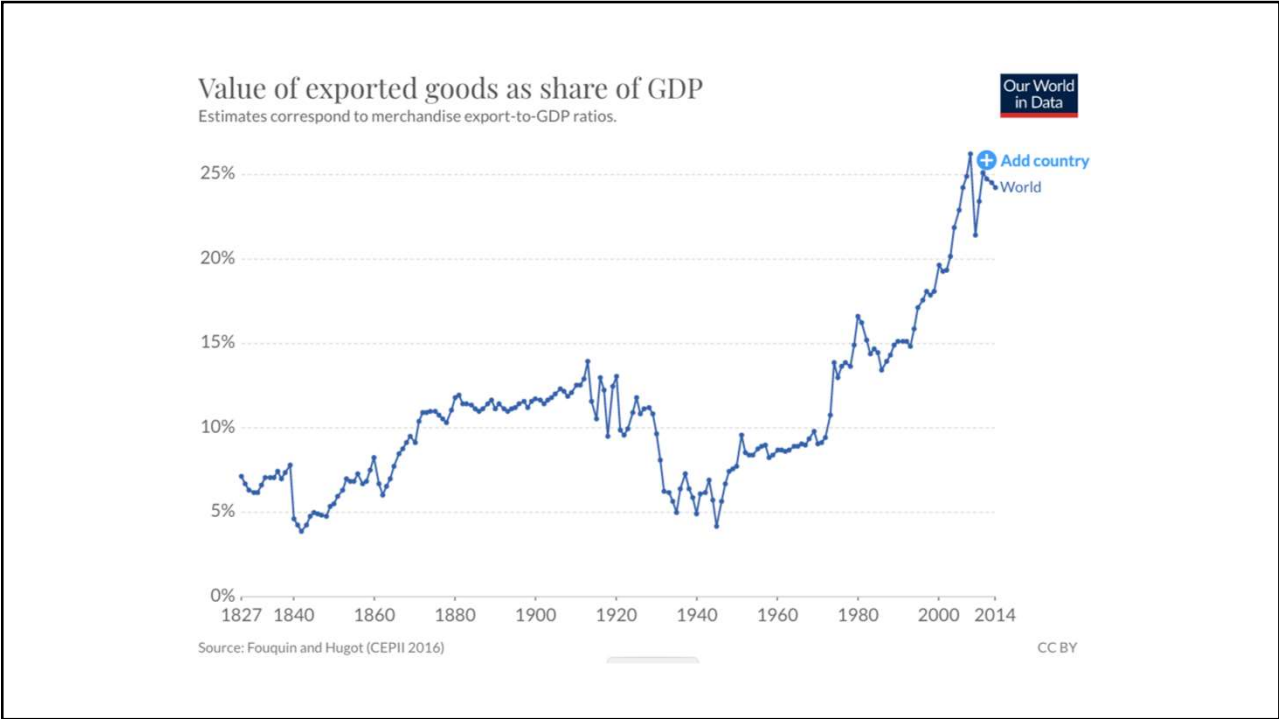
- **Growth over time of many interactions between countries**
 - Trade
 - Global Value Chains
 - Foreign Direct Investment
 - Financial Flows
 - International Travel
 - Migration
 - Telecommunications and transportation
- **I will focus here on trade**

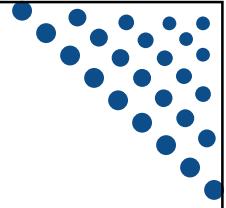
Trade



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Global Value Chains



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Effects on Economies

• Supply Chains

- Globalization has created long and complex international supply chains
- Pandemic and the war in Ukraine complicated them even more



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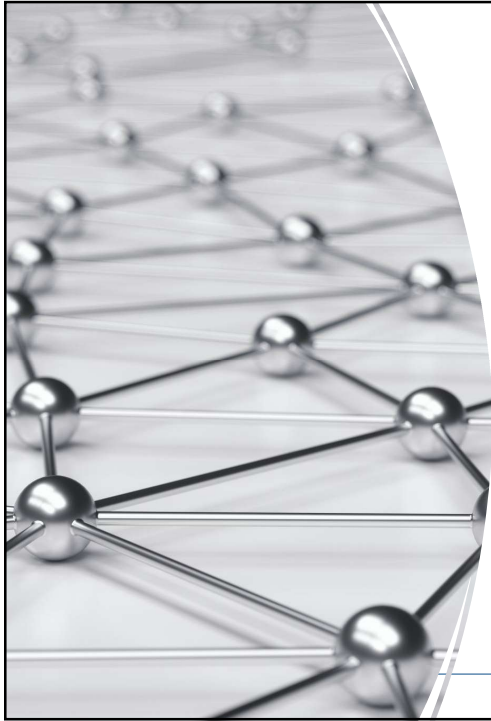


AV Trucks



- https://kodiak.ai/?gclid=CjwKCAjw_YShBhAiEiwAMomsEAFMEEMQh619kuR2L2NcZCQlt1NpQKwg_UsWFeQAM-yGvzfEW-MEIRoCeSkQAvD_BwE



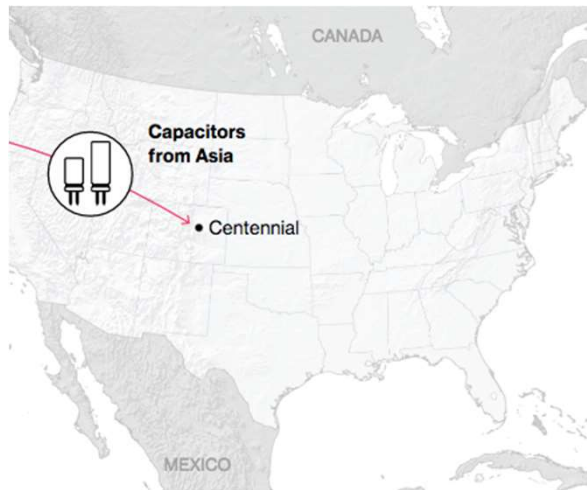


• Global Value Chains in Action

15



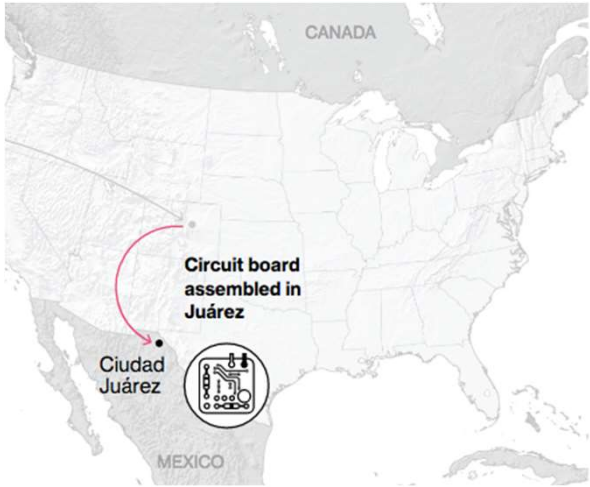
NAFTA and the Auto Supply Chain



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Black, Diamond, and Merrill, "One Tiny Widget's Dizzying Journey Shows Just How Critical Nafta Has Become," *Bloomberg*, February 2, 2017.

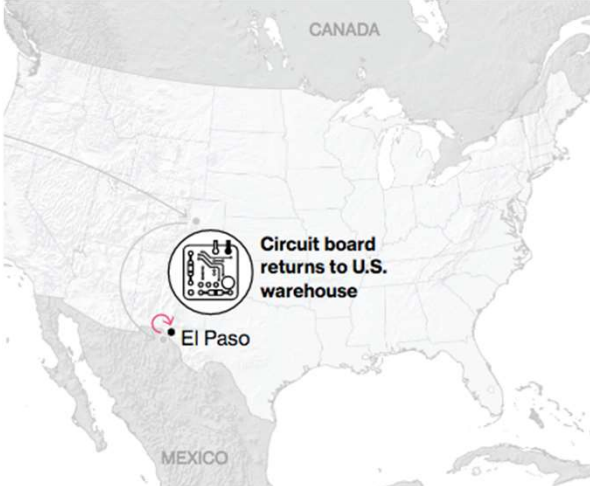
NAFTA and the Auto Supply Chain



A map of North America showing the United States, Canada, and Mexico. A red arrow points from a location in the United States to Ciudad Juárez, Mexico. A circular icon containing a circuit board is positioned near Ciudad Juárez. Text labels include "CANADA", "MEXICO", "Ciudad Juárez", and "Circuit board assembled in Juárez".

NATIO EDUCA Black, Diamond, and Merrill, "One Tiny Widget's Dizzying Journey Shows Just How Critical Nafta Has Become," *Bloomberg*, February 2, 2017.

NAFTA and the Auto Supply Chain

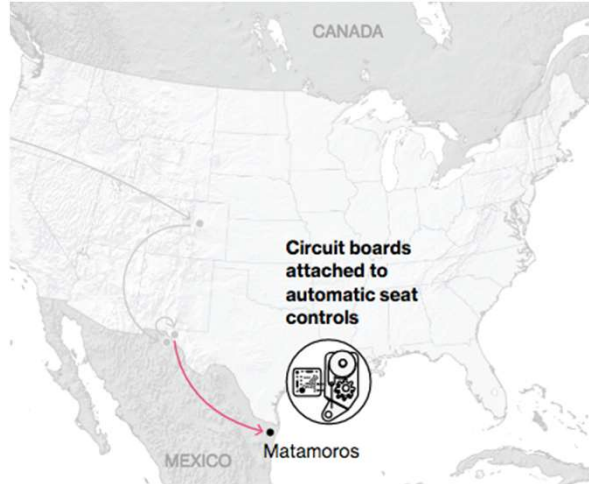


A map of North America showing the United States, Canada, and Mexico. A red arrow points from Ciudad Juárez, Mexico, to El Paso, Texas, in the United States. A circular icon containing a circuit board is positioned near El Paso. Text labels include "CANADA", "MEXICO", "El Paso", and "Circuit board returns to U.S. warehouse".

NATIO EDUCA Black, Diamond, and Merrill, "One Tiny Widget's Dizzying Journey Shows Just How Critical Nafta Has Become," *Bloomberg*, February 2, 2017.



NAFTA and the Auto Supply Chain



Black, Diamond, and Merrill, "One Tiny Widget's Dizzying Journey Shows Just How Critical Nafta Has Become," *Bloomberg*, February 2, 2017.




NAFTA and the Auto Supply Chain



Black, Diamond, and Merrill, "One Tiny Widget's Dizzying Journey Shows Just How Critical Nafta Has Become," *Bloomberg*, February 2, 2017.

NAFTA and the Auto Supply Chain

Seats installed at nearby auto assembly plants



Black, Diamond, and Merrill, "One Tiny Widget's Dizzying Journey Shows Just How Critical Nafta Has Become," *Bloomberg*, February 2, 2017.

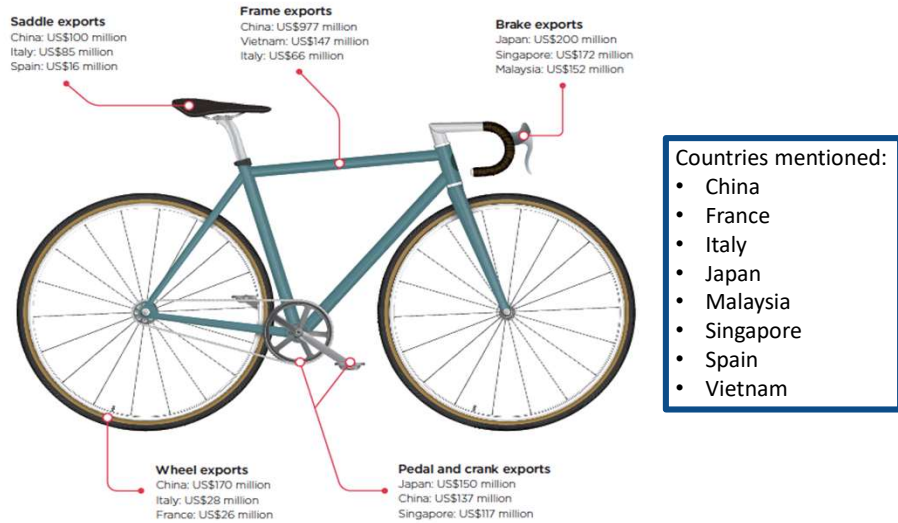
Growth of Global Value Chains, 1970-2015

Figure 1.2 GVC trade grew rapidly in the 1990s but stagnated after the 2008 global financial crisis

Year	GVC share of global trade (%)
1970	37
1975	40
1980	41
1985	41
1990	42
1995	45
2000	46
2005	48
2008	51
2010	50
2015	48

Source: World Development Report 2020

Figure 1.1 Where do bicycles come from?



Source: World Development Report 2020

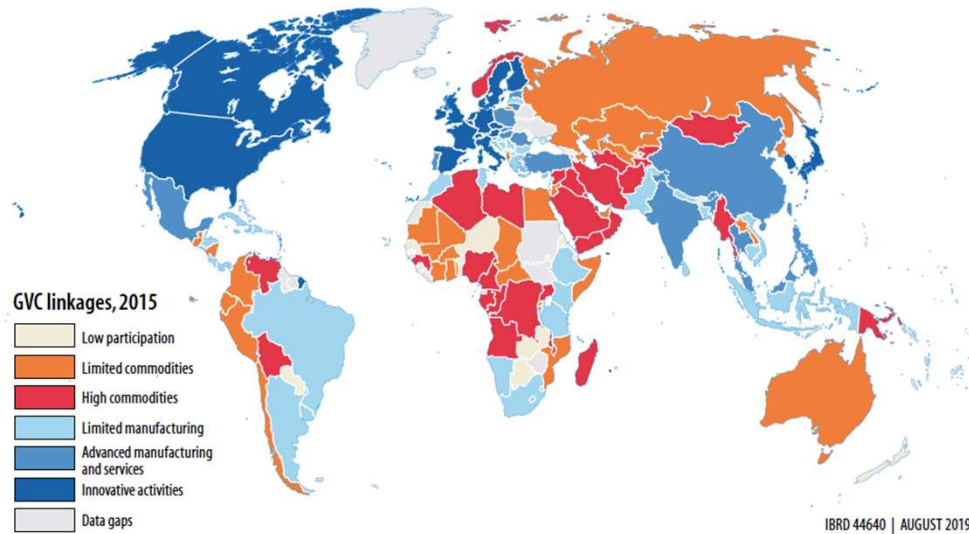
Supply Chains

• **Example: The iPhone assembled in China from parts:**

Part	Come from
Accelerometers	Germany, the US, South Korea, China, Japan, and Taiwan.
Audio chips	US, UK, China, South Korea, Taiwan, Japan, and Singapore.
Batteries	Samsung (South Korea), which has factories in eighty countries.
Cameras	Qualcomm (US) and Sony (Japan), both with plants in many countries
Chips for 3G/4G/LTE networking	Qualcomm (US)
Compasses	AKM Semiconductor (Japan) with plants in the US, France, England, China, South Korea, and Taiwan.
Glass screen	Corning (US) with plants in twenty-six countries.
Gyroscopes	Switzerland
... and many more	

Source: Krueger 2020, *International Trade (What Everyone Needs to Know)*, p. 254

Map 1.1 All countries participate in GVCs—but not in the same way

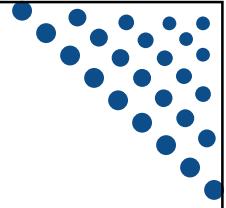


Source: World Bank

Pros and Cons of Globalization

• Pros and Cons of Globalization

- Gains from Trade
 - Theory of Comparative Advantage
 - Other Sources of Gain from Trade
- Costs of Trade



Gains from Trade

Theory of Comparative Advantage



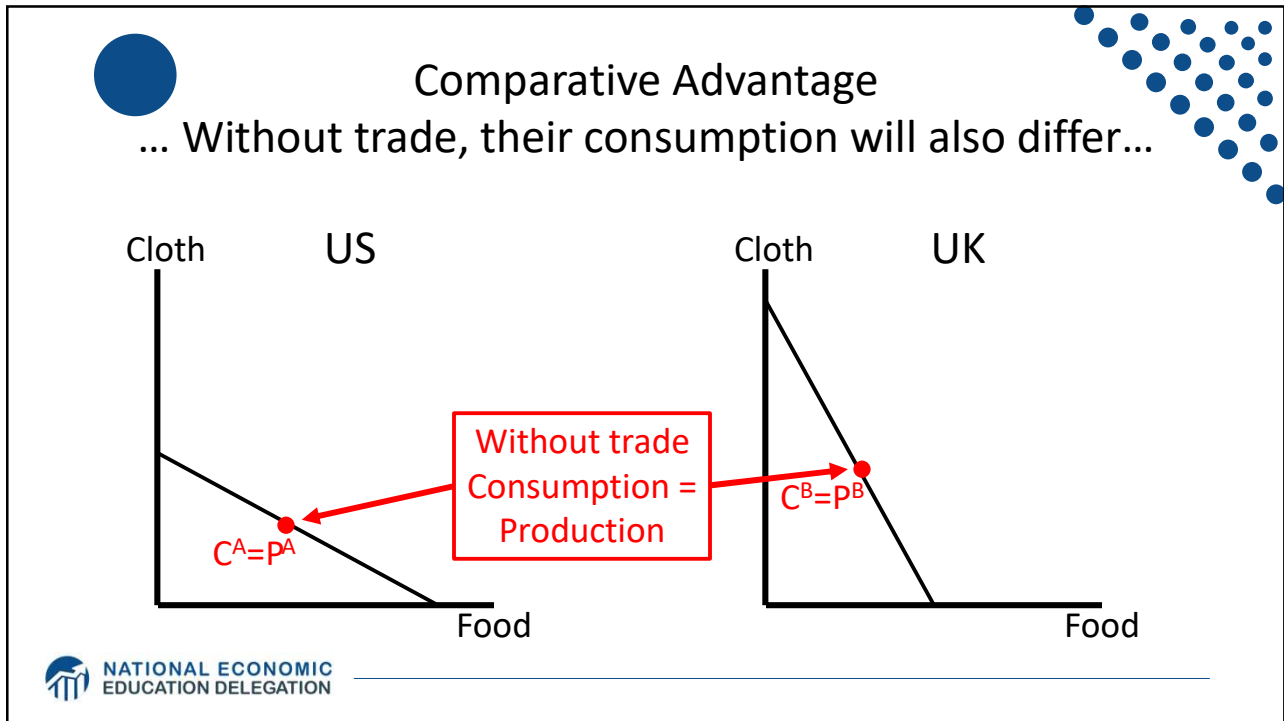
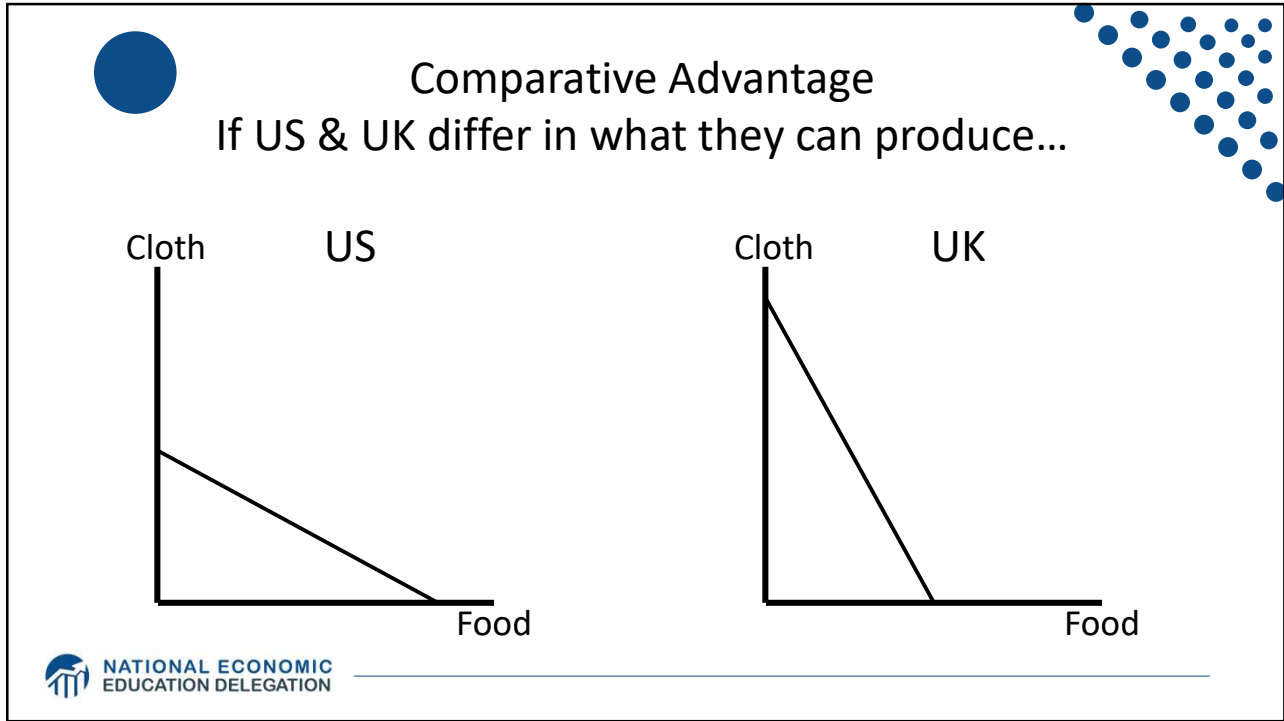
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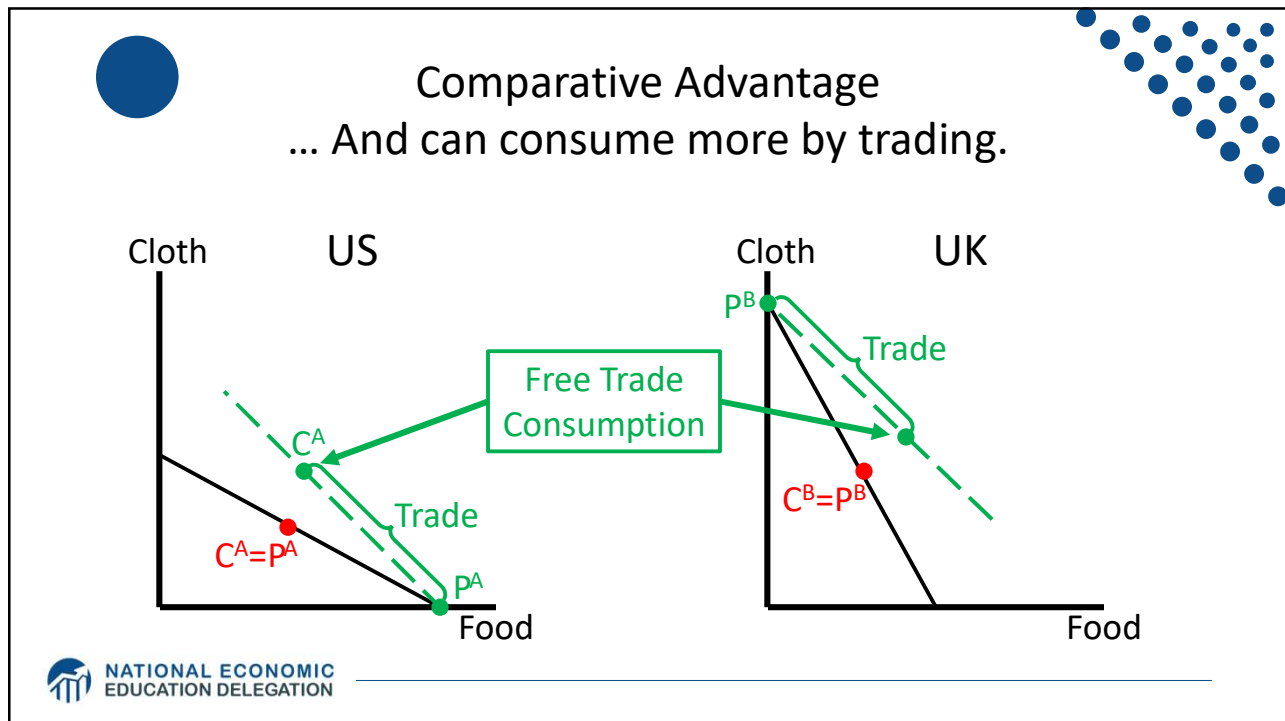
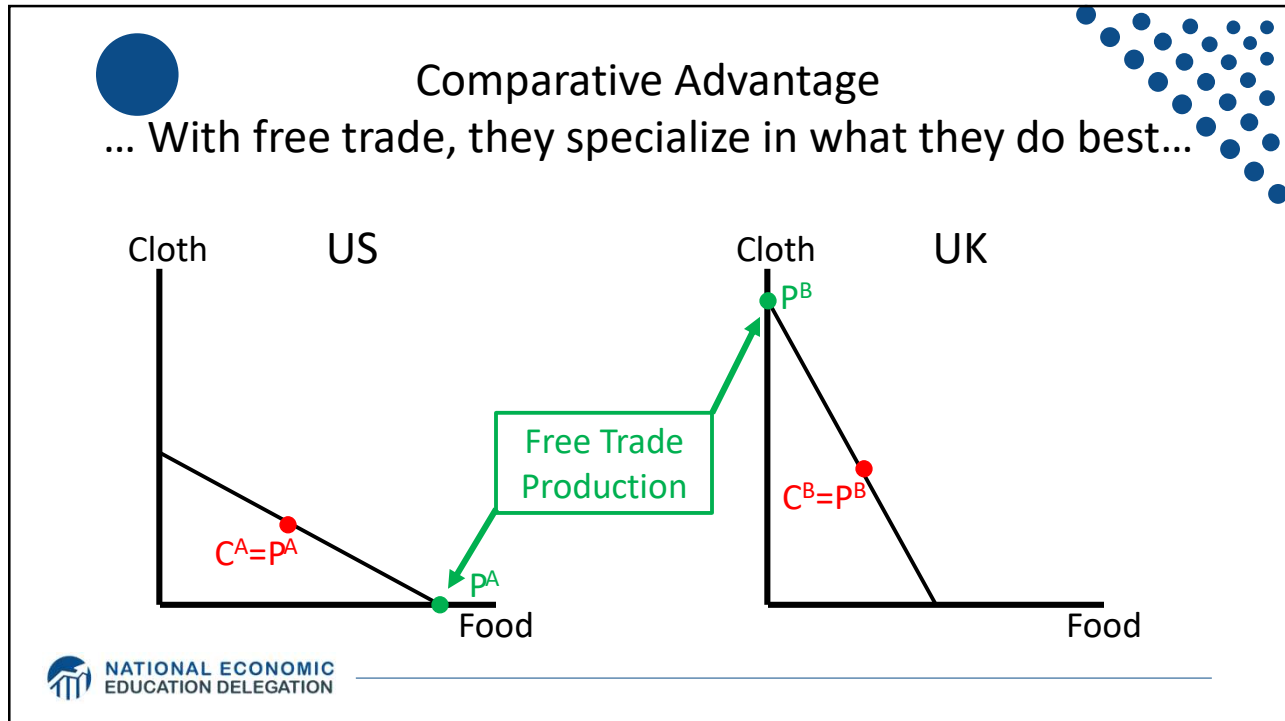
Comparative Advantage

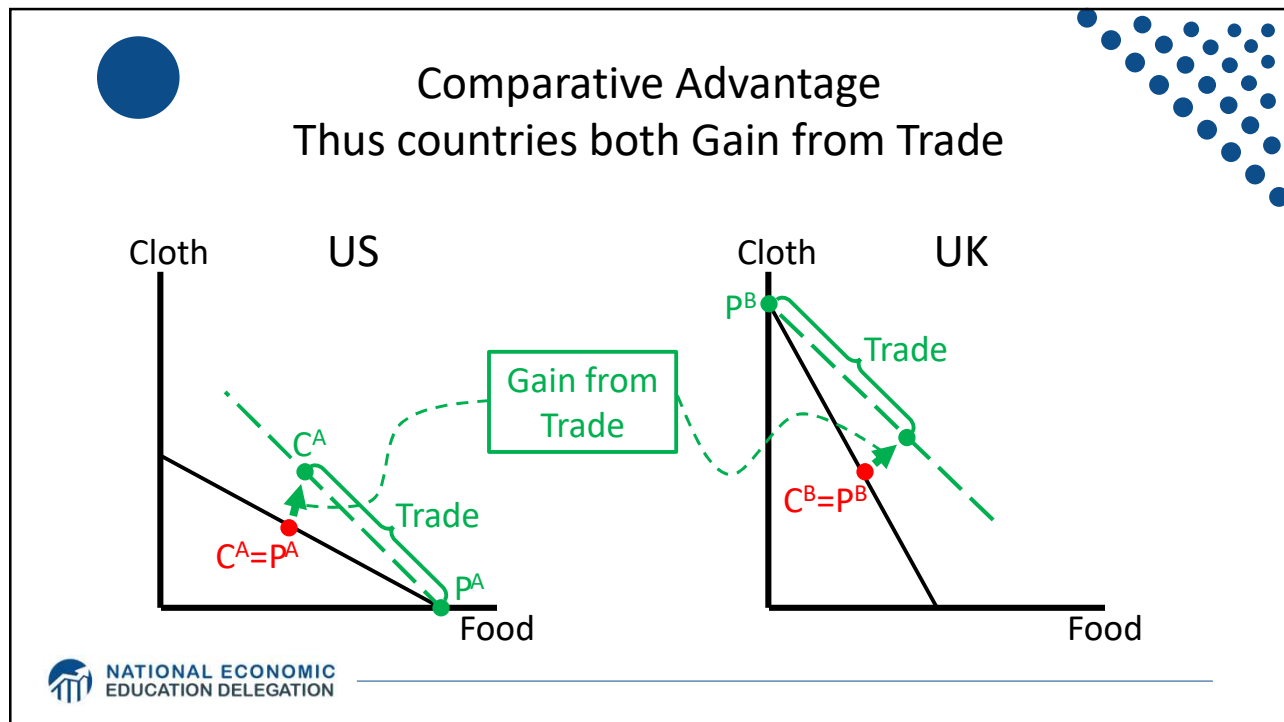
- **The Theory of Comparative Advantage says:**
 - Countries can, by producing
 - o More than they need of what they do relatively best, and
 - o Less than they need of what they do relatively worst
 - And exporting the extra to other countries in exchange for what they need
 - All countries can
 - o Get more of everything if that's what they want, and
 - o Gain from trade
- **Illustration with a graph of just 2 countries & 2 goods**
 - (I'm eager to know whether this helps you understand.)



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Generality of Comparative Advantage

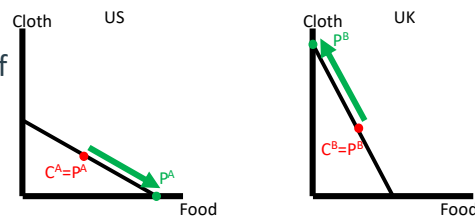
- **The Theory of Comparative Advantage requires:**
 - “Perfect competition” (i.e., all buyers and sellers are very small)
 - Absence of market “distortions” (externalities, etc.)
 - i.e., reasons why supplies and demands don’t reflect true costs and benefits
- **The Theory of Comparative Advantage does not require:**
 - Any limit on numbers of goods, factors, and countries
 - That only final goods are traded (thus consistent with supply chains)
 - That factors (labor, capital) be immobile between countries
 - (However, the gains from trade then accrue to countries including their mobile-factor owners.)

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Reality of Comparative Advantage

- **But note:**

- Nothing in the theory says that everyone in each country gains
- Opening to trade requires
 - Some industries to shrink or disappear while others expand
 - Firms and workers in shrinking industries
 - Certainly lose during the transition
 - May be permanently worse off
 - In example, losers are producers of
 - Cloth in US
 - Food in UK



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Gains from Trade

Other Sources of Gain from Trade



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Other sources of Gain from Trade

- **Productivity** (most productive firms expand and export)
- **Returns to scale** (small countries can support larger firms)
- **Competition** (monopolies in small countries lose market power)
- **Variety** (buyers can access more choices)
- **Supply chains** (firms can source parts from cheapest or best sources)
 - (That's really just the above, but within industries and firms.)
- **Technology** (producers get access foreign technologies)



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Costs of Trade



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But there are Costs

- **Economic:**
 - When trade expands (or contracts)
 - Some firms lose market share or shut down
 - Other firms supplying inputs shrink or shut down
 - Workers in both lose jobs
 - Their communities lose customers
 - Macroeconomic cost: Vulnerability to foreign recession/inflation
 - Dependence on other countries willingness to trade
 - Vulnerability to trade disruption
 - Crisis induced (earthquake, flood, disease)
 - Policy induced (sanctions, tariffs, export bans)
- **Non-economic**
 - Loss of cultural differences
 - Spread of disease



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Trade Policies that Affect Globalization

- **Policies that Encourage It**
 - Tariff Reductions
 - Trade Agreements
 - Other
- **Policies that Discourage It**
 - Tariffs
 - Trade War



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Policies that Encourage Globalization



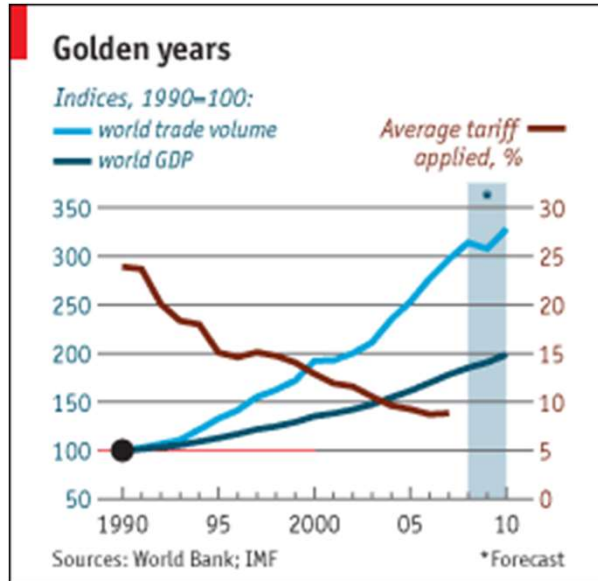
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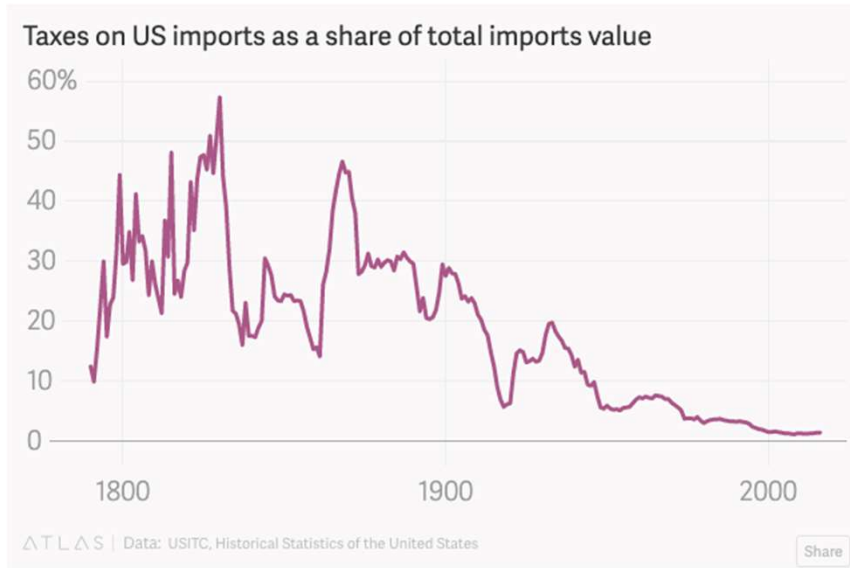
Tariff Reductions



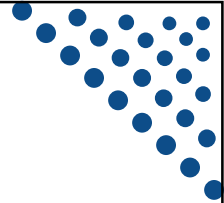
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Source: Economist



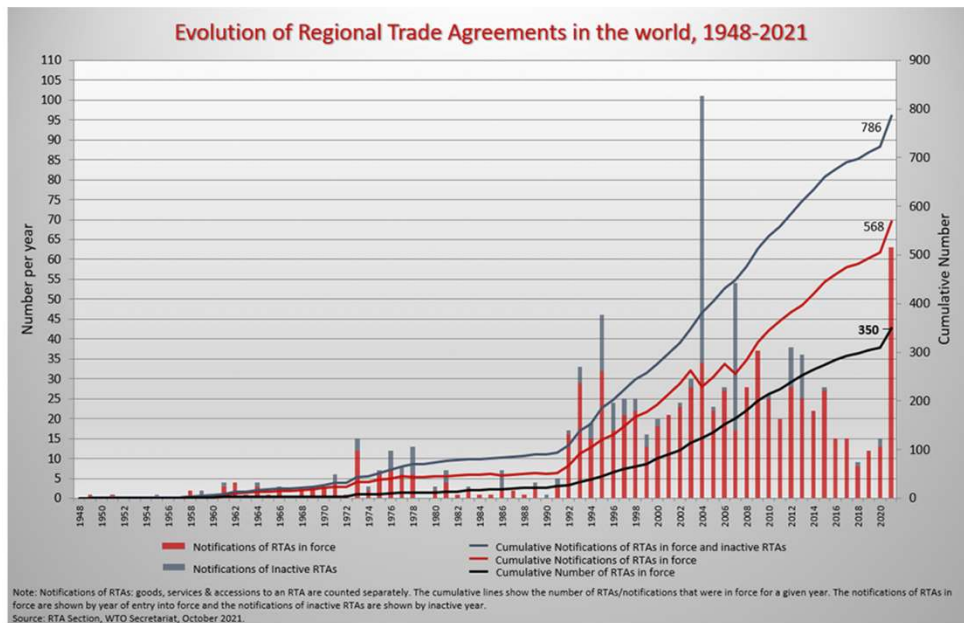
Source: Quartz 2018



Trade Agreements



Source:
WTO

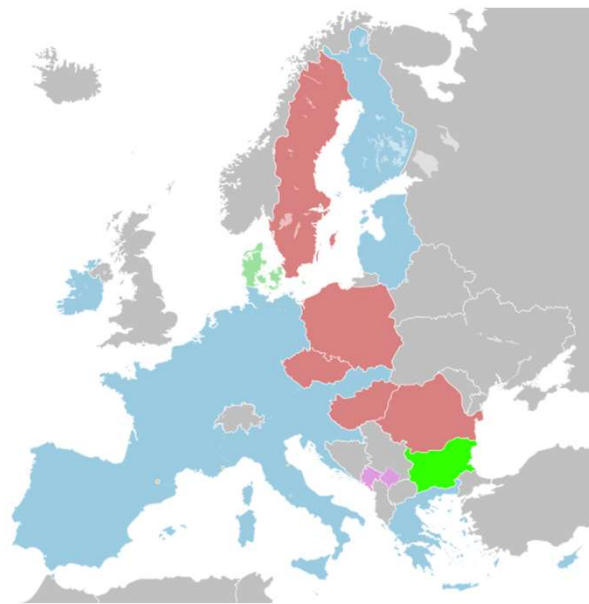


European Union



Source: Europa.eu

Eurozone



Source: Europa.eu

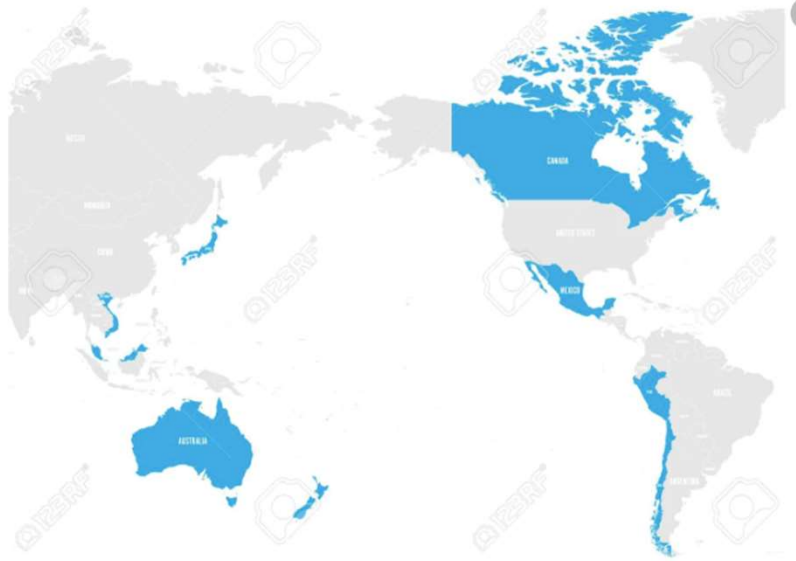
NAFTA (now USMCA)



MERCOSUR



CPTPP
=
**Trans-Pacific
Partnership
minus US
(US is
working to
re-engage)**



RCEP
=
**Regional
Comprehensive
Economic
Partnership**



Other Policies to Encourage Globalization

- **IMF/World Bank**

- Policy advice to open markets (the "Washington Consensus")
- Loans to countries conditional on
 - o Reducing trade barriers
 - o Permitting capital flows

- **GATT/WTO (World Trade Organization) [More on this later]**

- Negotiate reciprocal trade liberalization
- Settlement of trade disputes (usually about interfering with trade)

- **Bilateral Investment Treaties**

- Better treatment of multinational corporations



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Policies that Discourage Globalization

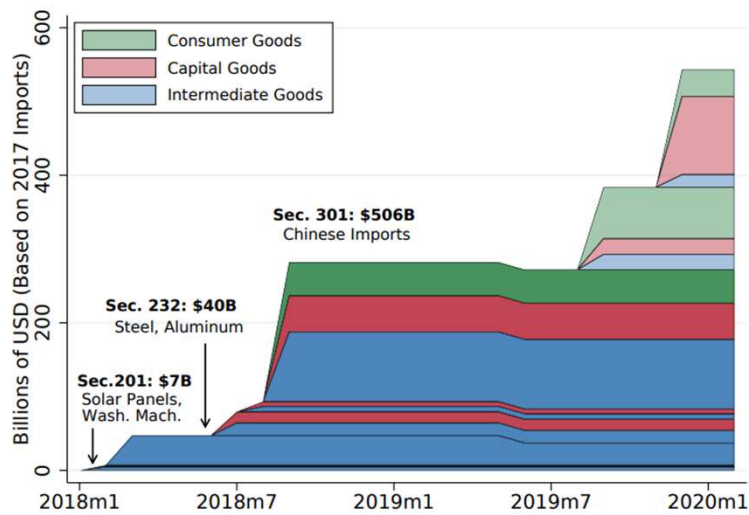


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Trump's Tariffs and Trade War

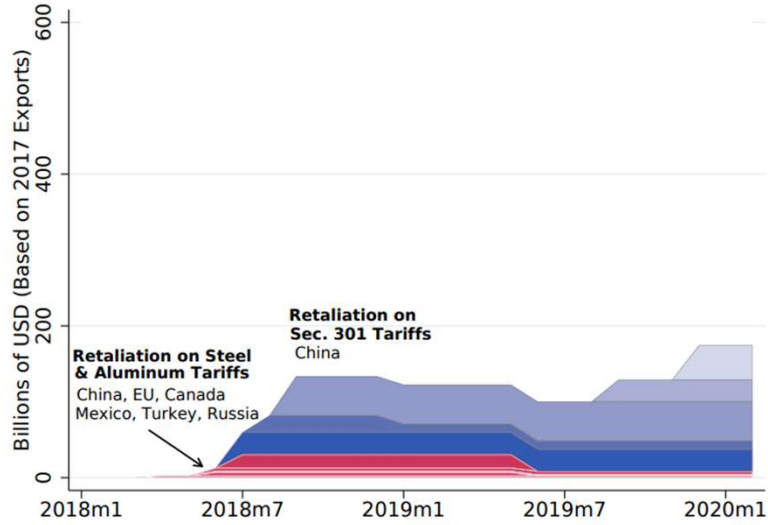


Figure B1: Composition of New U.S. Import Tariffs: 2018-2019

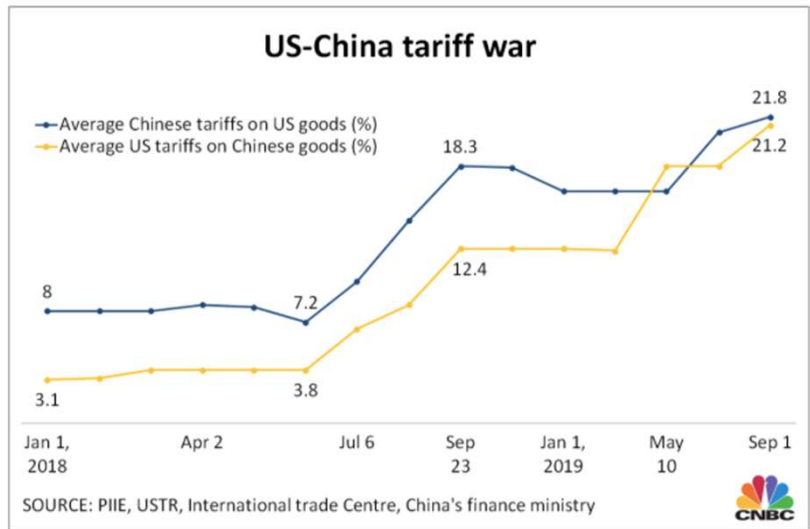


Source:
Flaan &
Pierce
2020

Figure 3: Timeline of Retaliatory Tariffs on U.S. Exports: 2018-2019



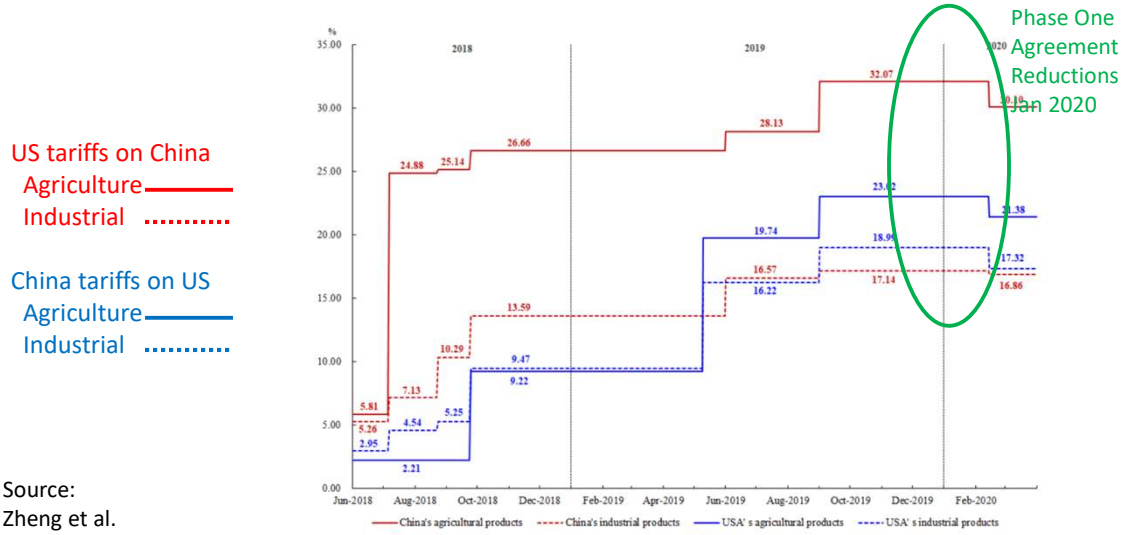
Source: Flaan & Pierce 2020



The first trade salvo was fired by the U.S. in early 2018, but the bilateral trade war between the U.S. and China really kicked into a higher gear in July 2018.

Source: CNBC.com

Figure 1. China-US bilateral import tariff increases, percentage points.



Source:
Zheng et al.
Oct 2021

Source: GTAP database and the list of additional tariffs published by China and the United States

Effects of Tariffs

Effects of a tariff

- **A tariff is a tax on imports. It causes:**
 - A rise in the price of the imported good in the importing country
 - A fall in the price of the imported good in the exporting country
 - The quantity imported to fall
 - The revenue of the tariff-levying government to rise
- **Almost always: the rise at home is much larger than the fall abroad**
 - That's especially true if importing country is small
 - But it's also true if importing country is large, such as U.S.
 - Example: Trump's tariffs caused US prices to rise, with hardly any perceptible fall in prices abroad.



Effects of a tariff

- **The rise in price in the importing country causes**
 - A rise in price of competing goods produced there
 - Benefits to those producers
 - Harm to buyers of both the import and the competing goods
 - Including producers that use the higher-priced goods as inputs
 - Their prices also rise, hurting their buyers
 - Employment changes
 - Increase in the protected industry
 - Decrease in industries that use imports as inputs
 - Example: Trump's 25% tariff on steel
 - Helps US steel firms and their workers
 - Hurts US auto firms and workers
 - and many other industries that use steel



Effects of a tariff

- **The fall in price in the exporting country causes**
 - Harm to sellers there
 - Benefit to buyers there
 - Shift of sales to other countries

- **If the tariff is on exports from only one country (e.g, China)**
 - Buyers shift to imports from other, more costly, countries (e.g., Vietnam)

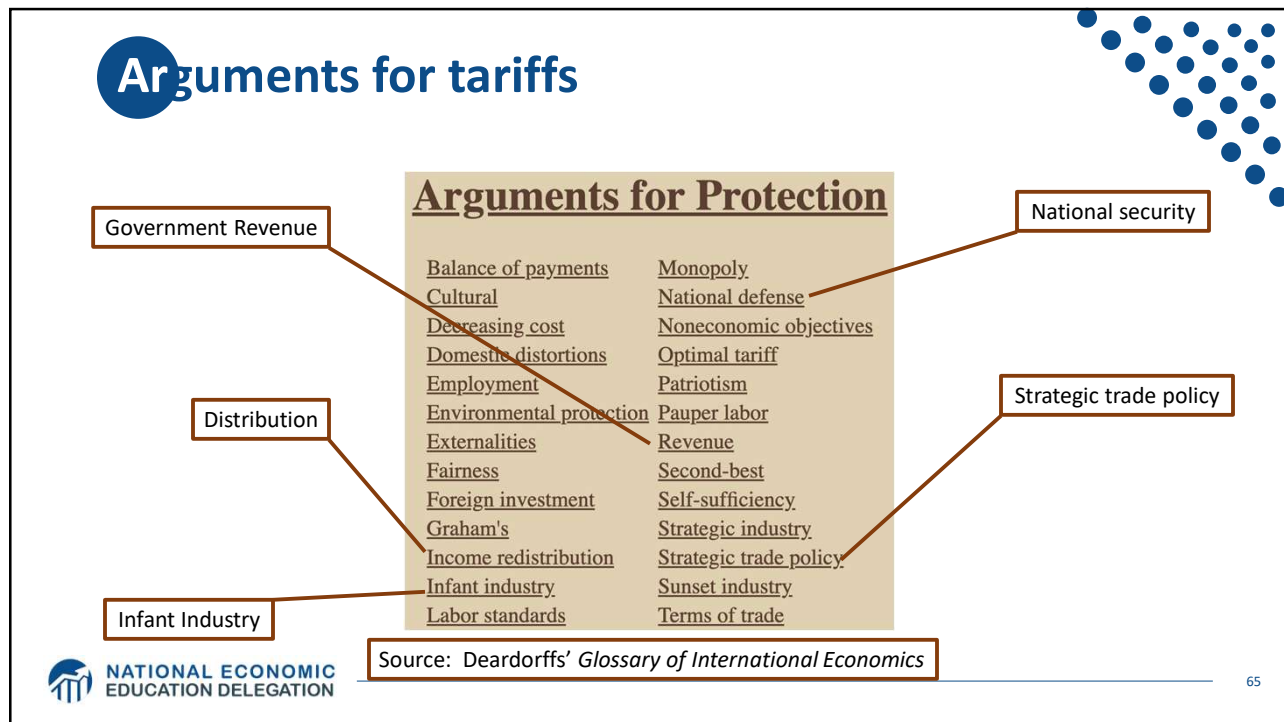


Arguments for and against tariffs

- **If economists are so opposed to tariffs, why are they used?**
- **Arguments for protection**
 - Many have been used, both past and present
 - See the list in A. Deardorffs' Glossary of International Economics (next)



Arguments for tariffs



Arguments against tariffs

• Arguments against tariffs

- Economic gains from trade (see above)
- Tariffs prompt retaliation
- Some valid arguments for tariffs depend on information that is either
 - o Unavailable, or
 - o Available only from the protected industry
- Even when net beneficial, tariffs are politically hard to remove
- Enables transfer of technology
- **Reduces likelihood of war**

The Role of Trade Agreements

- **Countries have negotiated trade agreements throughout history**
 - At least back to the 1500's between the Ottoman Empire and the powers of Europe
 - The first "free trade agreement" (FTA) was between Britain and France in 1860, soon followed by many more
 - Removed tariffs on trade with each other
 - US used "reciprocal trade agreements" starting in 1934 to reduce tariffs and dig out of the Great Depression
 - US led negotiation of multilateral agreements via
 - GATT (General Agreement on Tariffs and Trade) 1948
 - WTO (World Trade Organization) 1995

The Role of Trade Agreements

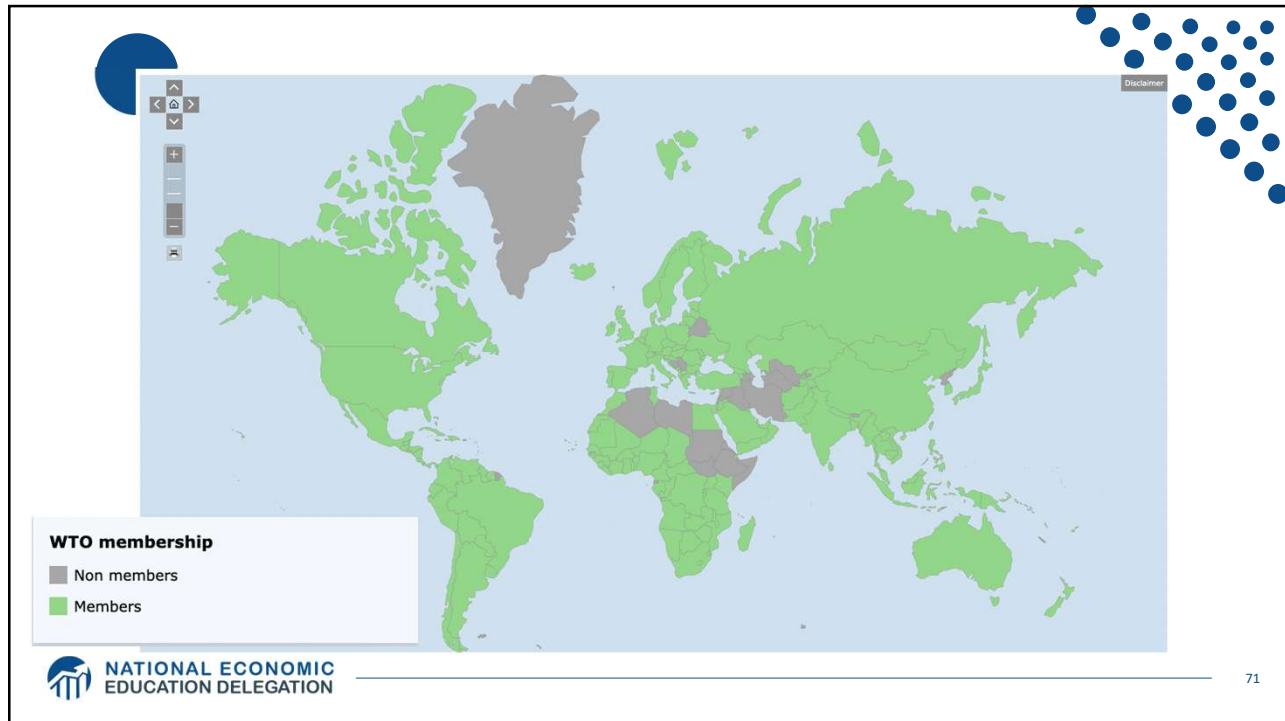
- **Trade Agreements (both WTO & FTAs)**
 - Promote trade by
 - Reducing tariffs
 - Blocking policies that discriminate against imports
 - But they also do much else, mostly to serve business interests:
 - Permit anti-dumping duties to deter competition
 - Protect intellectual property (patents, etc.)
 - Allow investor action against governments

The Role of Trade Agreements

- **WTO**

- 164 member countries
- Includes
 - China since 2001
 - Russia since 2012
 - Not Iran, N. Korea
- Headquarters Geneva, Switzerland





The Role of Trade Agreements

• The WTO has

- Three Parts:

1. GATT (Still exists, as largest part of WTO)
 - limits tariffs
2. GATS = General Agreement on Trade in Services
3. TRIPs Agreement = Trade Related aspects of Intellectual Property Rights

- Two Basic Principles

1. Most Favored Nation
2. National Treatment

The Role of Trade Agreements

• The WTO's Main Functions

- Negotiation of reduced trade barriers
 - Tariffs (GATT did this well; WTO not)
 - Removal of other barriers
- Dispute settlement
 - Countries bring cases against others
 - WTO "panels" and "Appellate Body" decide

The Role of Trade Agreements

• WTO Dispute Settlement

- There have been 609 cases initiated since 1995 (as of 1/30/22)
- About 90% have been decided in favor of the complainant, both by (132) and against US (168)
- The mechanism has been unable to decide cases since December 10, 2019 when
 - President Trump blocked appointments to Appellate Body
 - President Biden has not changed this

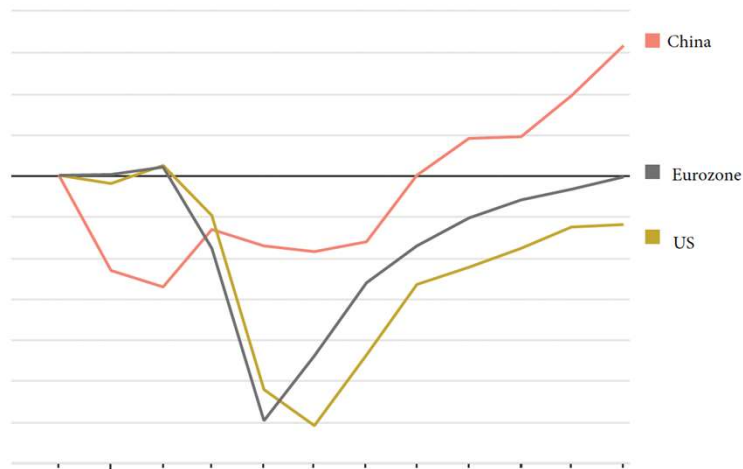
Effects of the Pandemic

• Effects of the Pandemic on Economies

- Travel halted
- Stock markets fell but came back strongly
- Factories shut down
- Supply chains were interrupted
- Trade plummeted but came back



Change in export volumes, since December 2019



Source:
Hannon, WSJ,
Feb 25, 2021

Notes: Seasonally adjusted; at 2010 prices
Source: CPB Netherlands Bureau for Economic Policy Analysis

The Pandemic and Globalization

• Trade and Covid-19

- Globalization helped it spread
- Trade in PPE and medical supplies helped to fight it
- Trade in vaccines is essential globally
- Trade policies have often interfered



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The War and Globalization

• Trade and the War in Ukraine

- War related trade
- Non-war related trade
 - Consumer goods
 - Oil and gas
 - Food supply and prices



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Globalization's Future?



Globalization's Future?

- **Will trade, travel, etc. come back?**
 - Yes.
- **Will it reach the previous trend**
 - Most likely
 - It didn't after the financial crisis
- **Will attitudes change?**
 - Yes.
 - Firm's will try to limit exposure
 - Consumers will learn to live differently
- **Will economists' views of globalization change?**
 - I think so.
 - o We still think globalization is good,
 - o But we're learning that it needs to include greater protections for those who are hurt.

International Institutions: Alan Deardorff Next Week



Thank you!

Any Questions?

www.NEEDecon.org

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