



Osher Lifelong Learning Institute, Fall 2022

Contemporary Economic Policy Issues

American University
Fall, 2022

Jon Haveman, Ph.D.
National Economic Education Delegation



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Course Outline

- **Contemporary Economic Policy**

- Week 1 (9/23): Economic Update (Jon Haveman, NEED)
- **Week 2 (9/30): Trade and Globalization (Alan Deardorff, University of Michigan)**
- Week 3 (10/7): Autonomous Vehicles (Jon Haveman, NEED)
- Week 4 (10/14): Climate Change Economics (Sarah Jacobson, Williams College)
- Week 5 (10/21): The Federal Debt (Joseph Carolan, Oakland University)
- Week 6 (10/28): Trade Deficit and Exchange Rates (Alan Deardorff, Univ. of Michigan)



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Submitting Questions

- **Please submit questions of clarification in the chat.**
 - I will try to handle them as they come up.
- **We will do a verbal Q&A once the material has been presented.**
- **OLLI allowing, we can stay beyond the end of class to have further discussion.**
- **Slides will be available from the NEED website tomorrow (https://needelegation.org/delivered_presentations.php)**

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Trade and Globalization

Alan V. Deardorff
University of Michigan

Presentation to Osher Lifelong Learning Institute
American University
September 30, 2022

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Impact of Russia-Ukraine War

- **How Russia-Ukraine war impacts globalization**
 - War itself disrupts trade, especially exports of
 - Ukraine: wheat
 - Russia: wheat, oil
 - Economic sanctions by governments disrupt
 - Financial linkages
 - Trade
 - Private companies stop dealing with Russia

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Impact of Russia-Ukraine War

• Financial sanctions by US, EU, UK, and others

- Frozen foreign-held assets of individuals, Putin and dozens of others
- Restrictions on Russia's Central Bank's use of international reserves
- Several Russian banks removed from the Swift international payments system
- Cut off many Russian banks from transactions and operations
- Long list of Russian companies banned or restricted
- Possible restrictions on Russia borrowing from IMF and World Bank



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Impact of Russia-Ukraine War

• Trade sanctions by governments

- Oil and other energy
 - o Germany puts Nord Stream 2 gas pipeline on hold
 - o US bans from Russia
 - o UK to phase out Russian oil by end of 2022
 - o EU to become independent from Russia by 2030
- EU bans steel imports from Russia
- US restricts exports to Russia, especially technology and military; later also to Belarus; later also luxury goods
- EU and UK impose export restrictions similar to US
- Ban on Russian air carriers by Canada, EU, US, UK
- G-7 to revoke Russia's most favored nation status
 - o Permits them to raise tariffs on Russian goods

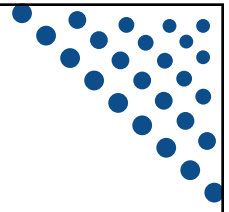


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Russia Sanctions, Gov't

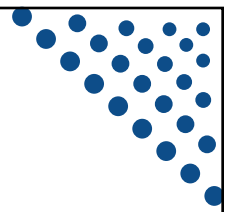


Countries		
Australia	Iceland	Singapore
Bahamas	Italy	Switzerland
Canada	Japan	Taiwan
EU	New Zealand	UK
Finland	Norway	US
France	Poland	
Germany	S Korea	

Source: Funakoshi et al, "Updated July 7, 2022" but includes from July 29



Russia Sanctions, Gov't



Russian Targets						
Airlines	2	Generals	1	Oligarchs	23	
Banks	9	Government	1	Retail	1	
Cnt. Banks	5	Lawmakers	2	Ships	5	
Commodity	1	Lux. goods	1	Sv with fnd	1	
Companies	19	Media	2	Tax service	1	
Economy	3	Mil. Comps.	14	Tech	1	
Entities	3	Mining	2	Transit	1	
Finance	1	Oil	2			
Gas	1	Oil imports	6			

Source: Funakoshi et al, "Updated July 7, 2022" but includes from July 29



Russia Sanctions, Gov't

- Countries announcing they will not use sanctions against Russia:

NOT using sanctions	
India	Feb 24
Mexico	Mar 1
Brazil	Mar 1
China	Mar 2
Argentina	Mar 4
Indonesia	Mar 9
Turkey	Mar 13
S Africa	Mar 17
Serbia	Apr 21

Source: Bown



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Impact of Russia-Ukraine War

- Private Companies Stop Dealing in Russia, per NBC News updated Mar 16:
 - Automotive: Ford, GM, Toyota, ...
 - Aviation: Airbus, Boeing, American, Delta, United, ...
 - Energy: BP, ExxonMobil, Shell
 - Equipment: Caterpillar, Honeywell, Deere
 - Food & Bev: Burger King, Coke, McDonalds, Starbucks, ...
 - Finance: Citigroup, Deutsche Bank, Vanguard, ...
 - Consumer goods: Proctor & Gamble, Unilever, Mars, ...
 - Leisure: Airbnb, Hilton, Expedia, ...
 - Logistics: DHL, FedEx, Maersk, UPS
 - Media: Netflix, Roku, Disney, ...
 - Payment services: Amex, Visa, Western Union, ...
 - And many more: Consulting, Retail, Technology



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Leaving Russia

253 companies, including ...

Source: New York Times, April 7, 2022

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Suspending activity

248 companies, including ...

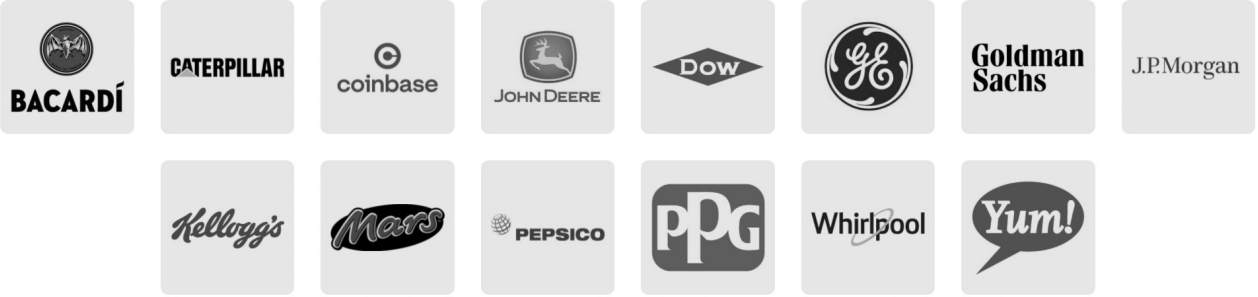
Sold all stores May 20. Stores will operate under new brand.

Source: New York Times, April 7, 2022

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Scaling back activity

75 companies, including ...



Source: New York Times, April 7, 2022

15

Halting investments

96 companies, including ...



Source: New York Times, April 7, 2022

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Staying the course

162 companies, including ...



Source: New York Times, April 7, 2022

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Effect of Sanctions

- **Too soon to know fully**

- Will they stop Russia?
 - o Clearly no, or at least not yet
 - o Sanctions in the past have only sometimes worked
- Will they reduce trade?
 - o They already have
 - o But Russia's role in trade is not large in most products
 - o Short-term effects are greater from the war itself

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Outline

- **What is Globalization?**
- **Pros and Cons of Trade**
- **Trade Policies**
- **The Role of Trade Agreements & WTO (if time)**

What Globalizations Is

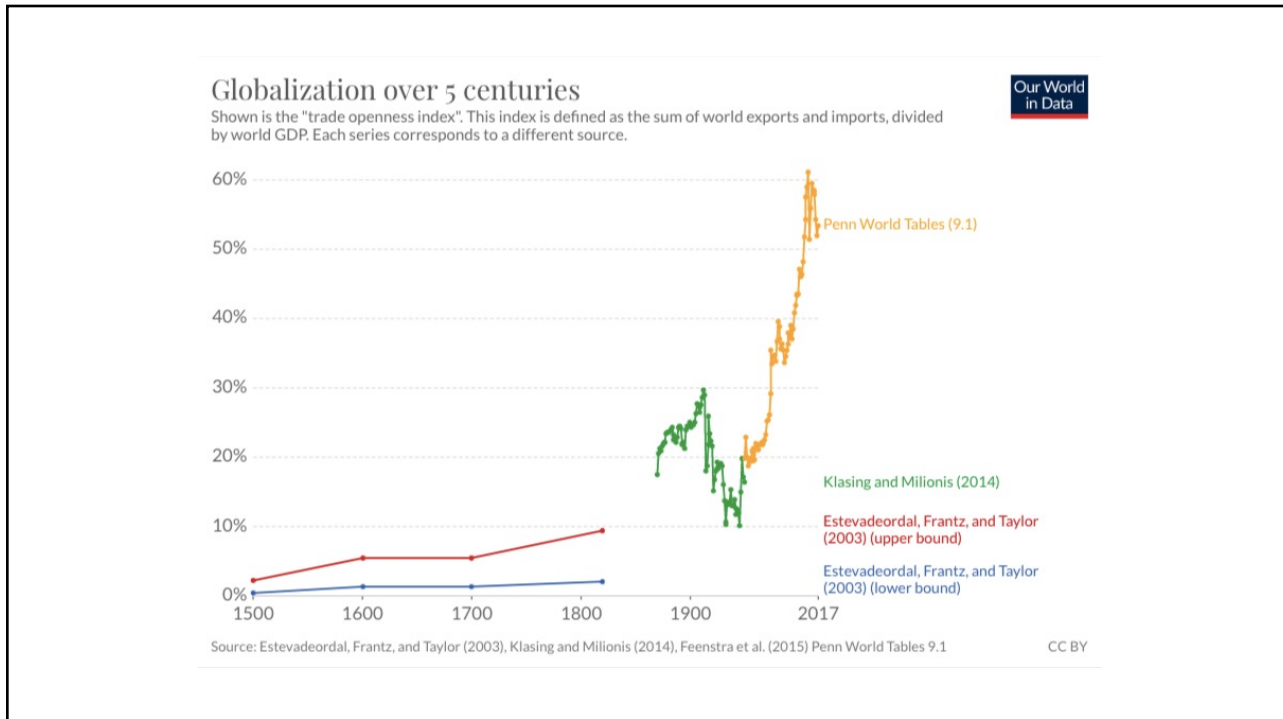
- **Growth over time of many interactions between countries**
 - Trade
 - Global Value Chains
 - Foreign Direct Investment
 - Financial Flows
 - International Travel
 - Migration
- **I will focus here on trade**

Trade

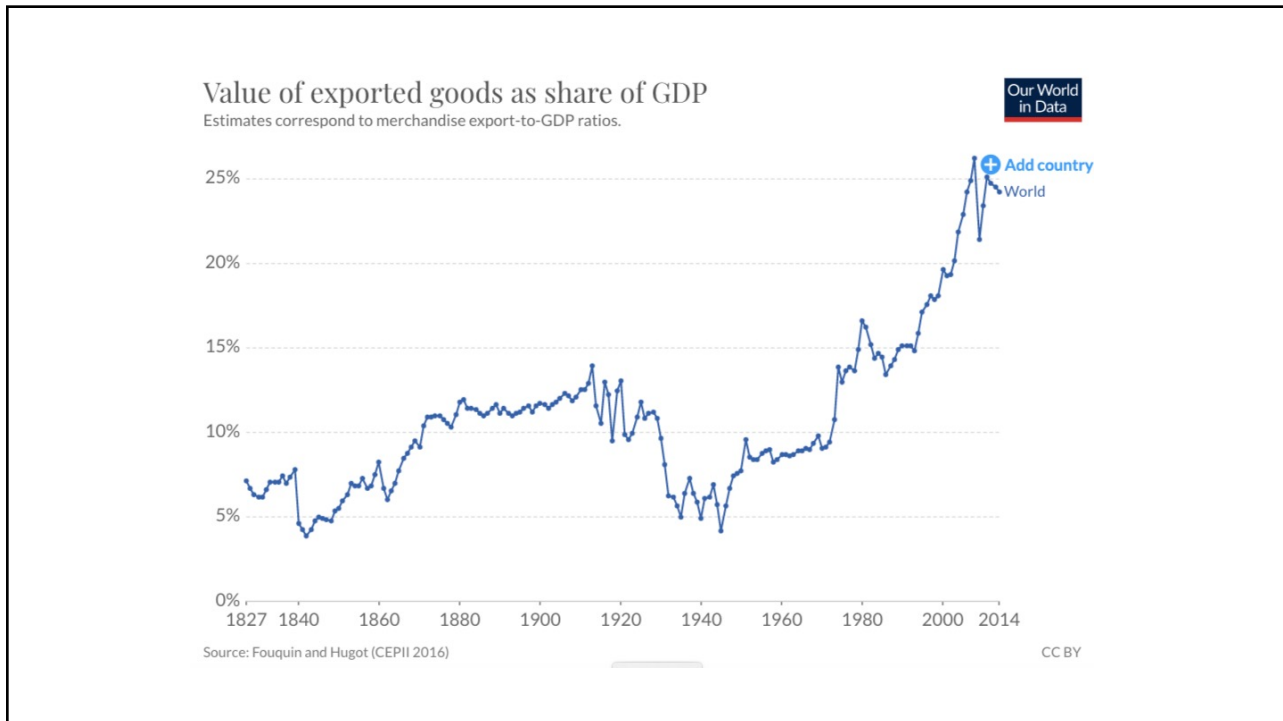


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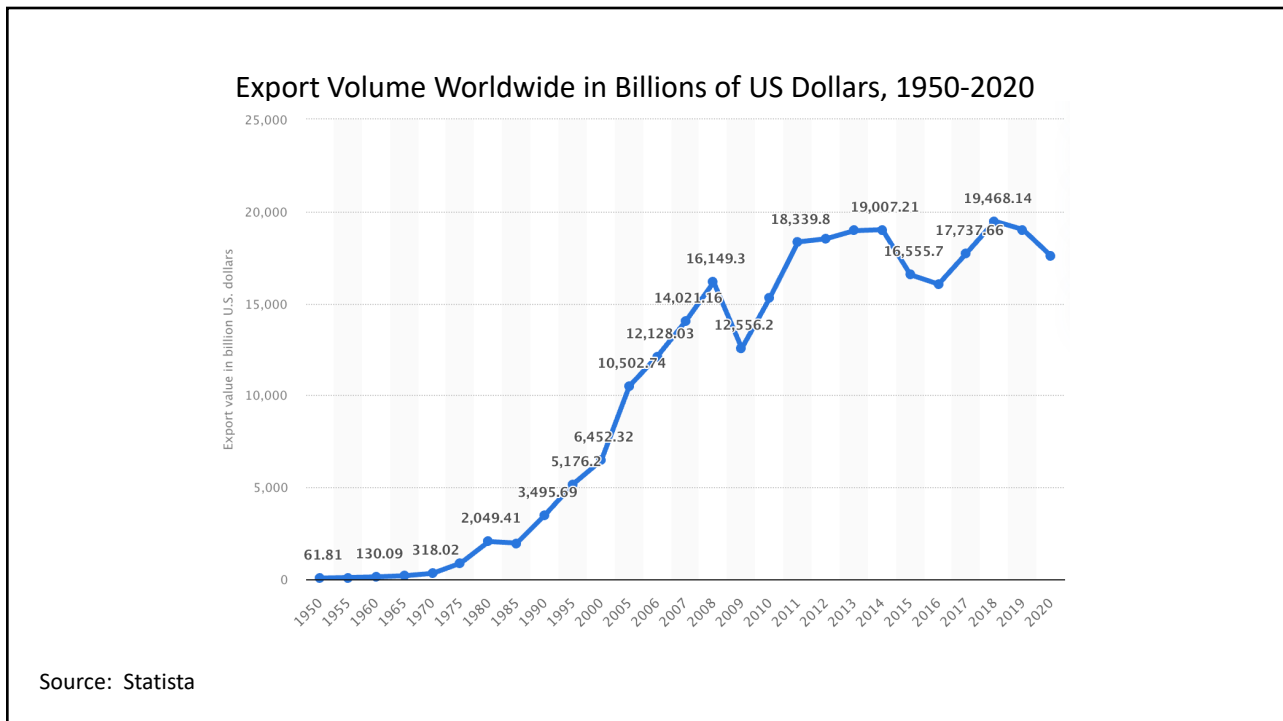
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Global Value Chains



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Effects on Economies

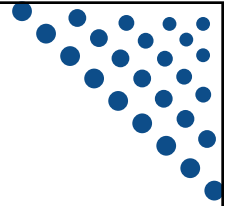
- **Supply Chains**
 - Globalization has created long and complex international supply chains



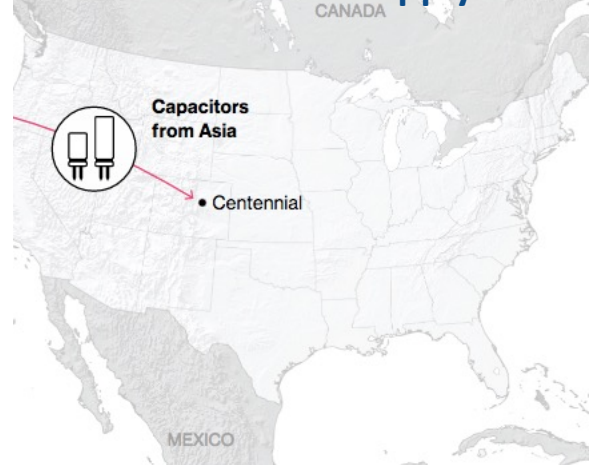
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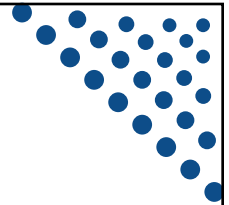
NAFTA and the Auto Supply Chain



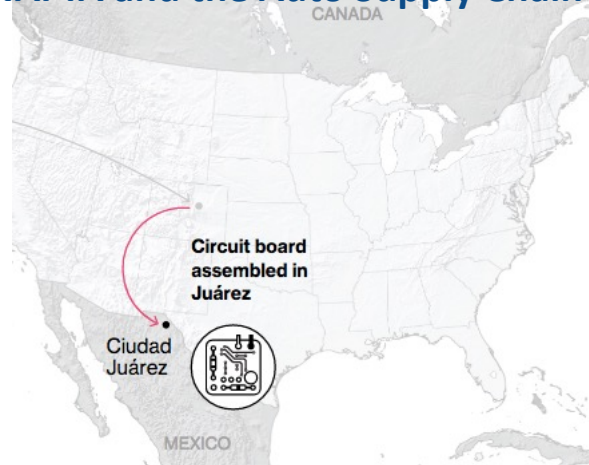
Black, Diamond, and Merrill, "One Tiny Widget's Dizzying Journey Shows Just How Critical Nafta Has Become," *Bloomberg*, February 2, 2017.

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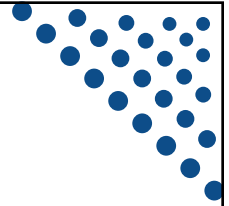
NAFTA and the Auto Supply Chain



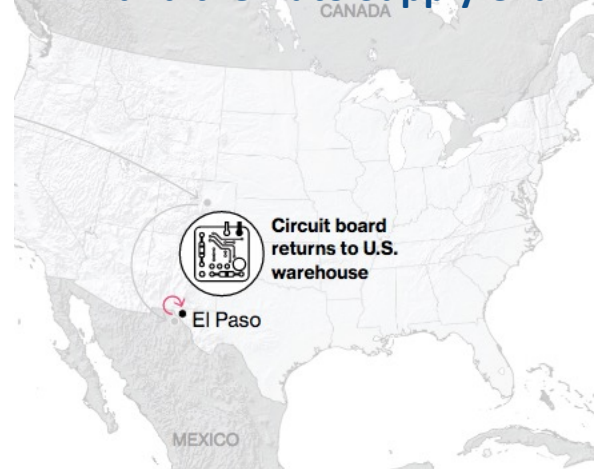
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NAFTA and the Auto Supply Chain

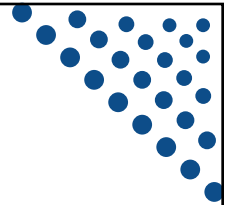


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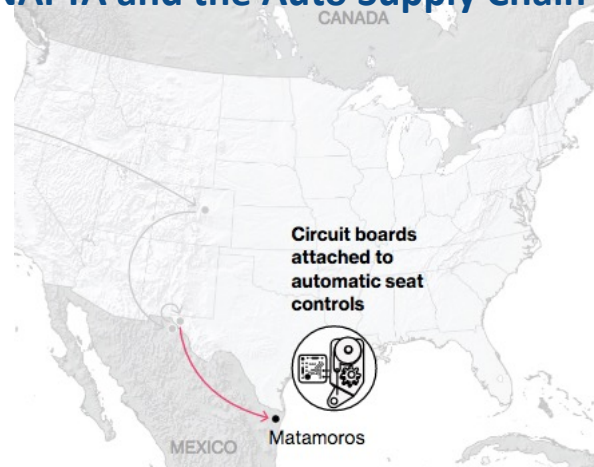
Black, Diamond, and Merrill, "One Tiny Widget's Dizzying Journey Shows Just How Critical Nafta Has Become," *Bloomberg*, February 2, 2017.

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NAFTA and the Auto Supply Chain

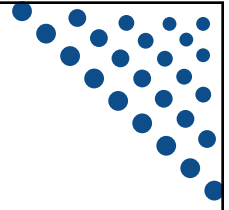


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Black, Diamond, and Merrill, "One Tiny Widget's Dizzying Journey Shows Just How Critical Nafta Has Become," *Bloomberg*, February 2, 2017.

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NAFTA and the Auto Supply Chain

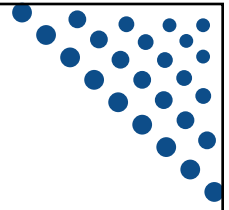


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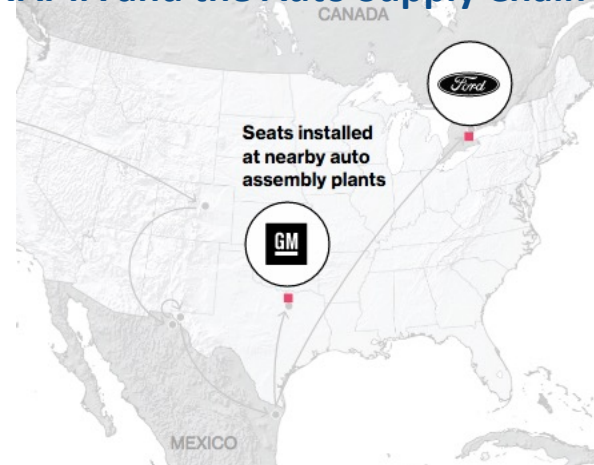
Black, Diamond, and Merrill, "One Tiny Widget's Dizzying Journey Shows Just How Critical Nafta Has Become," *Bloomberg*, February 2, 2017.

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NAFTA and the Auto Supply Chain



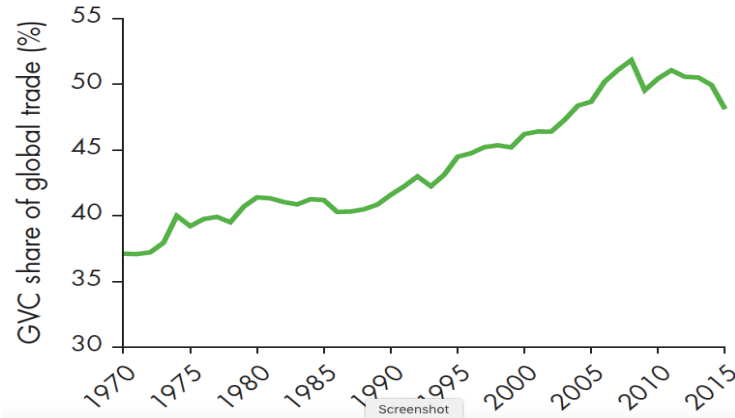
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Black, Diamond, and Merrill, "One Tiny Widget's Dizzying Journey Shows Just How Critical Nafta Has Become," *Bloomberg*, February 2, 2017.

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Growth of Global Value Chains, 1970-2015

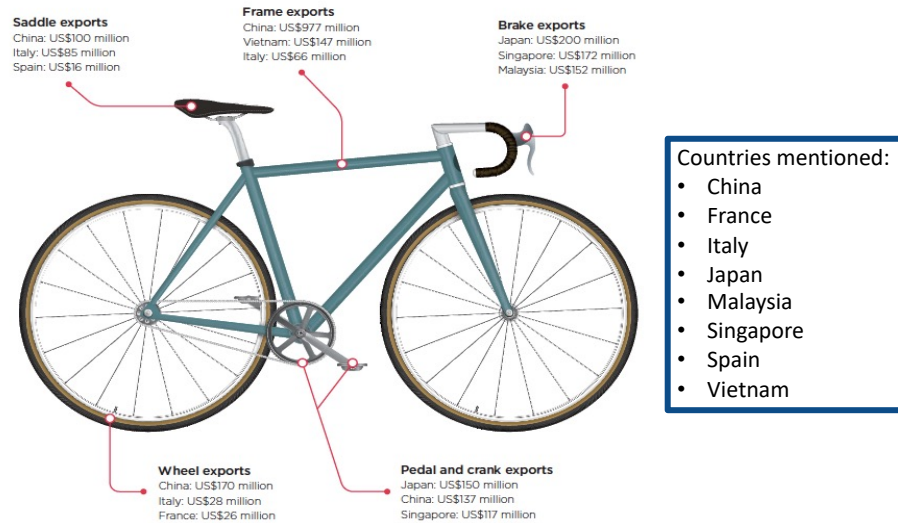
Figure 1.2 GVC trade grew rapidly in the 1990s but stagnated after the 2008 global financial crisis



Source: World Development Report 2020

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Figure 1.1 Where do bicycles come from?



Source: World Development Report 2020

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Supply Chains

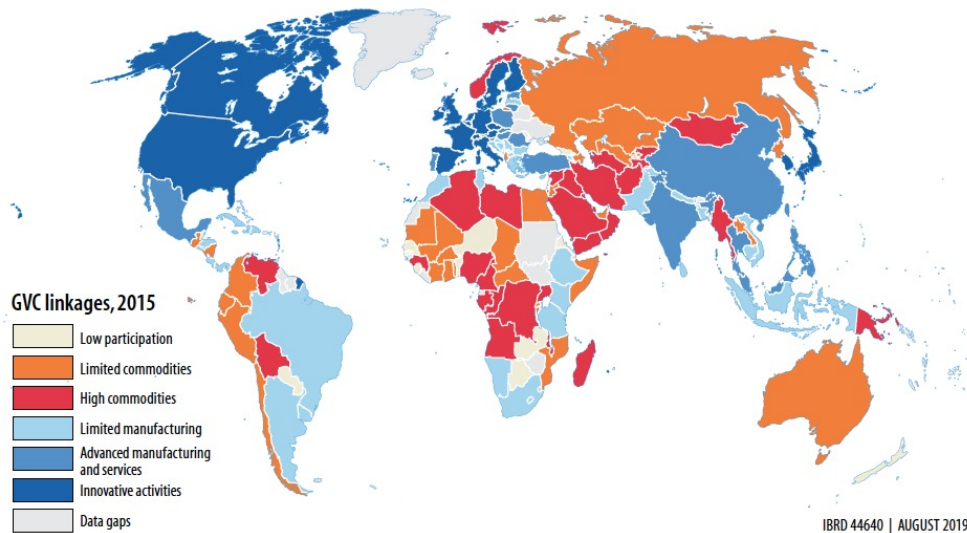
• Example: The iPhone assembled in China from parts:

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



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Gains from Trade

Theory of Comparative Advantage



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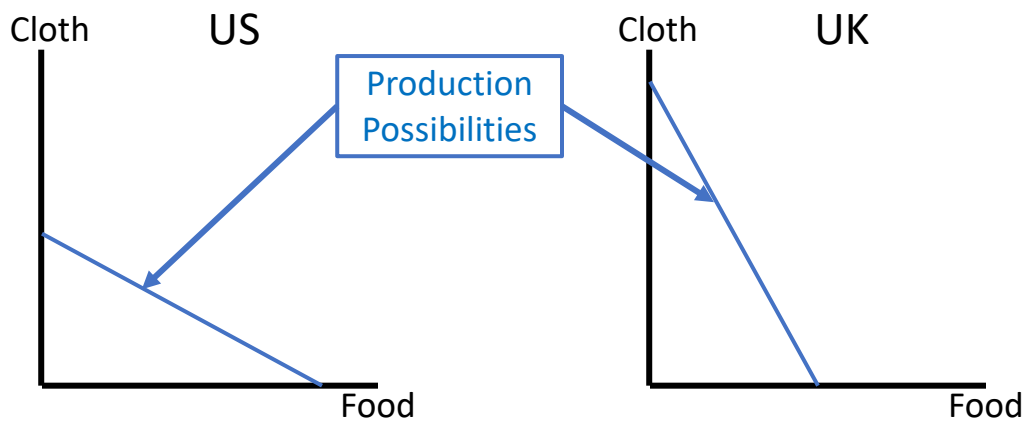
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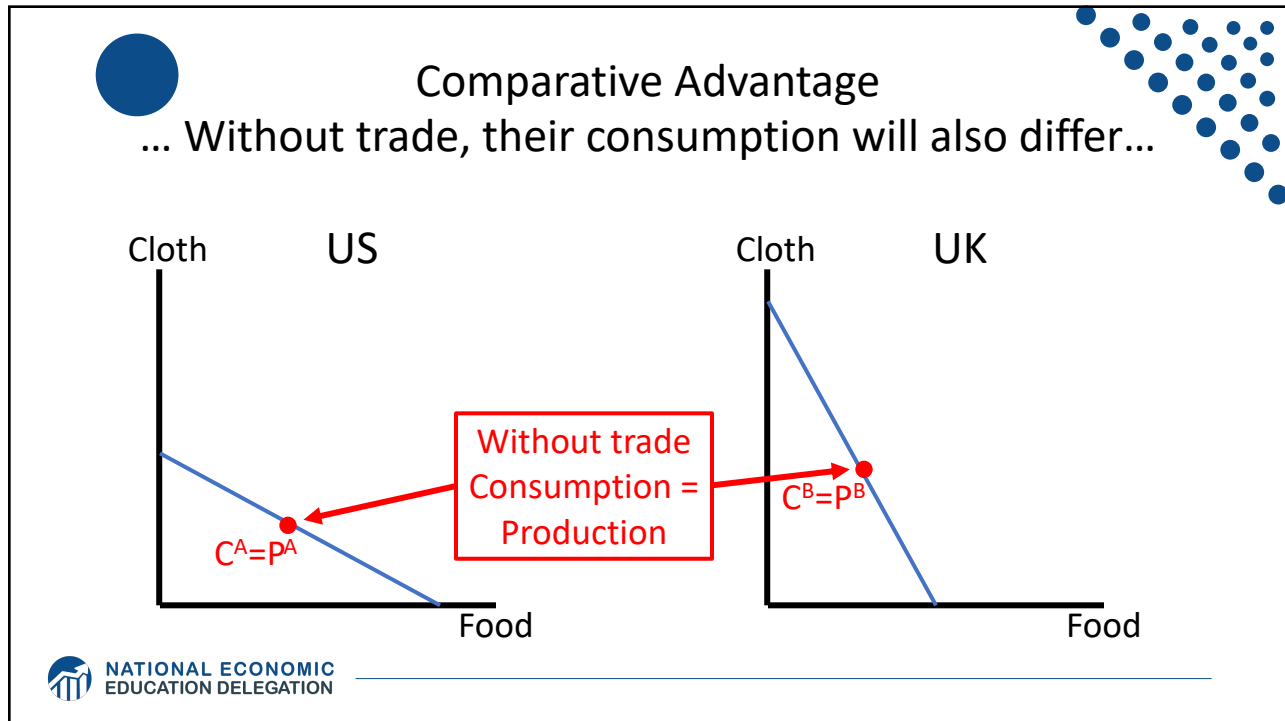
Comparative Advantage

- **The Theory of Comparative Advantage says:**
 - Countries can gain,
 - o By producing
 - More than they need of what they do relatively best, and
 - Less than they need of what they do relatively worst
 - o And exporting the extra to other countries in exchange for what they need
 - By doing that, ALL countries can
 - o Get more of everything, if that's what they want, and therefore
 - o Gain from trade
- **Illustration with a graph of just 2 countries & 2 goods**

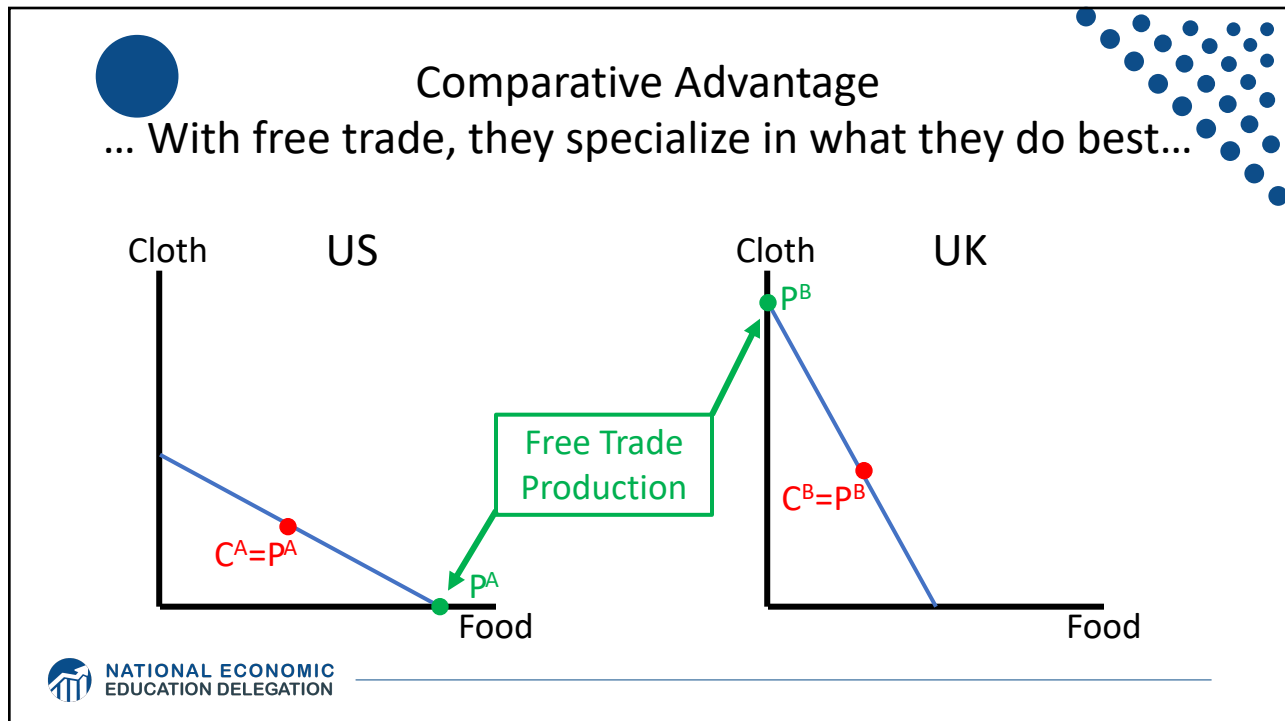


Comparative Advantage If US & UK differ in what they can produce...

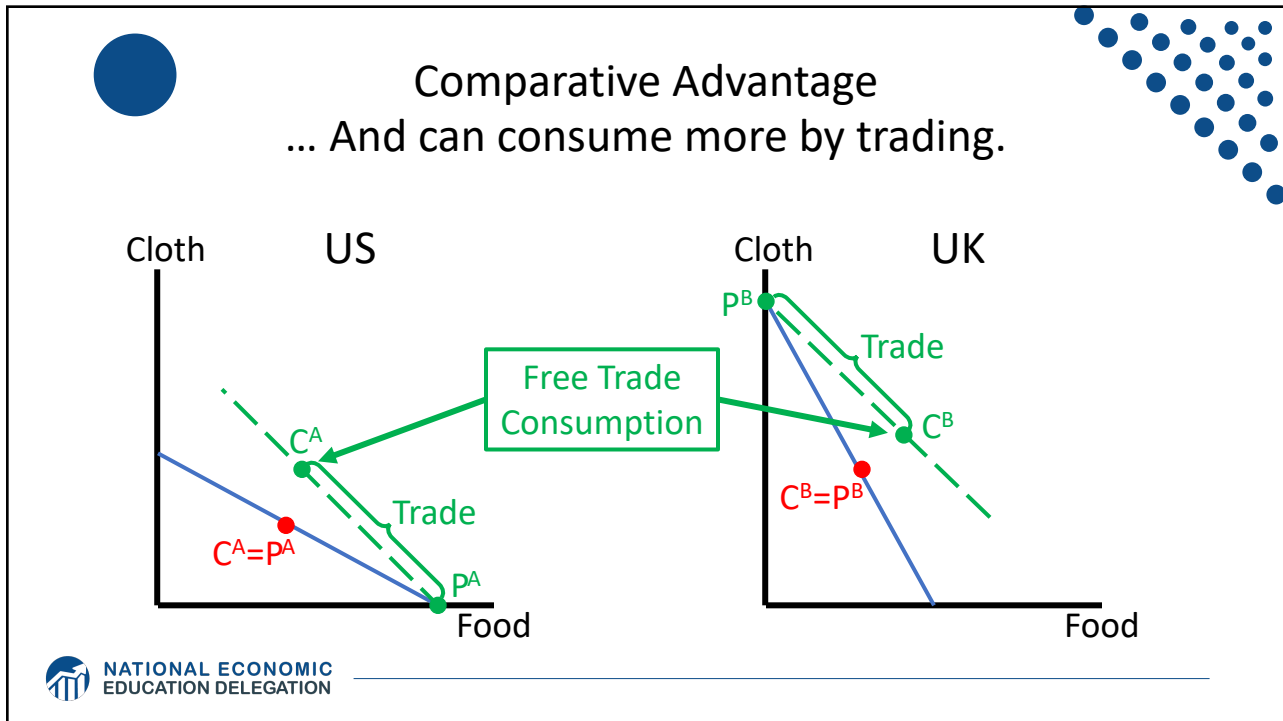




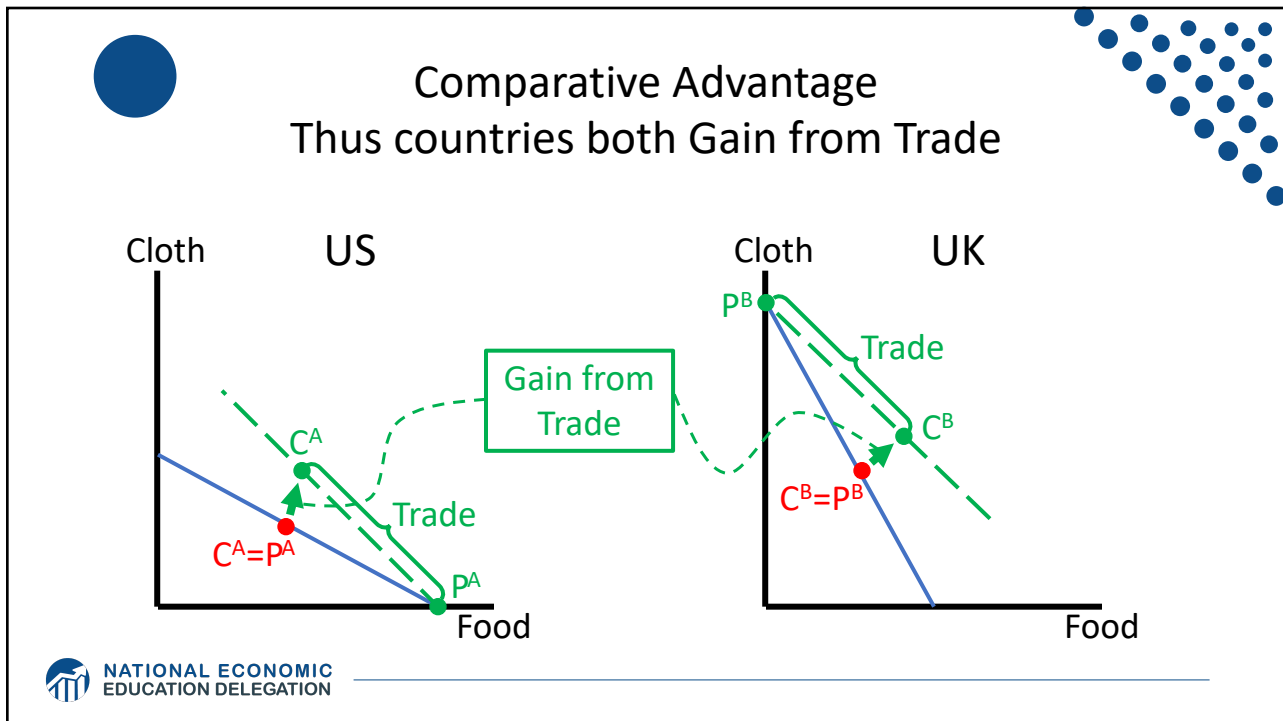
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Generality of Comparative Advantage

- **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.)



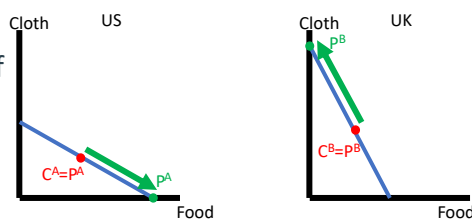
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Generality of Comparative Advantage

- **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, both consumers and firms, 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)
 - o Some firms lose market share or shut down
 - o Other firms supplying inputs to those firms shrink or shut down
 - o Workers in both lose jobs
 - o And their **communities** lose customers
- Macroeconomic cost: Vulnerability to foreign recession/inflation
- Dependence on other countries' willingness to trade
- Vulnerability to trade disruption
 - o Crisis induced (earthquake, flood, disease, war)
 - o Policy induced (sanctions, tariffs, export bans)

- **Non-economic**

- Loss of cultural differences
- Spread of invasive species and plant disease
- Spread of human disease



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Pause

- **Pause for**
 - Questions
 - 5-Minute Break
- **Next: Trade Policies**



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Trade Policies that Affect Globalization

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



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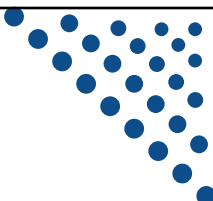



Policies that Encourage Globalization




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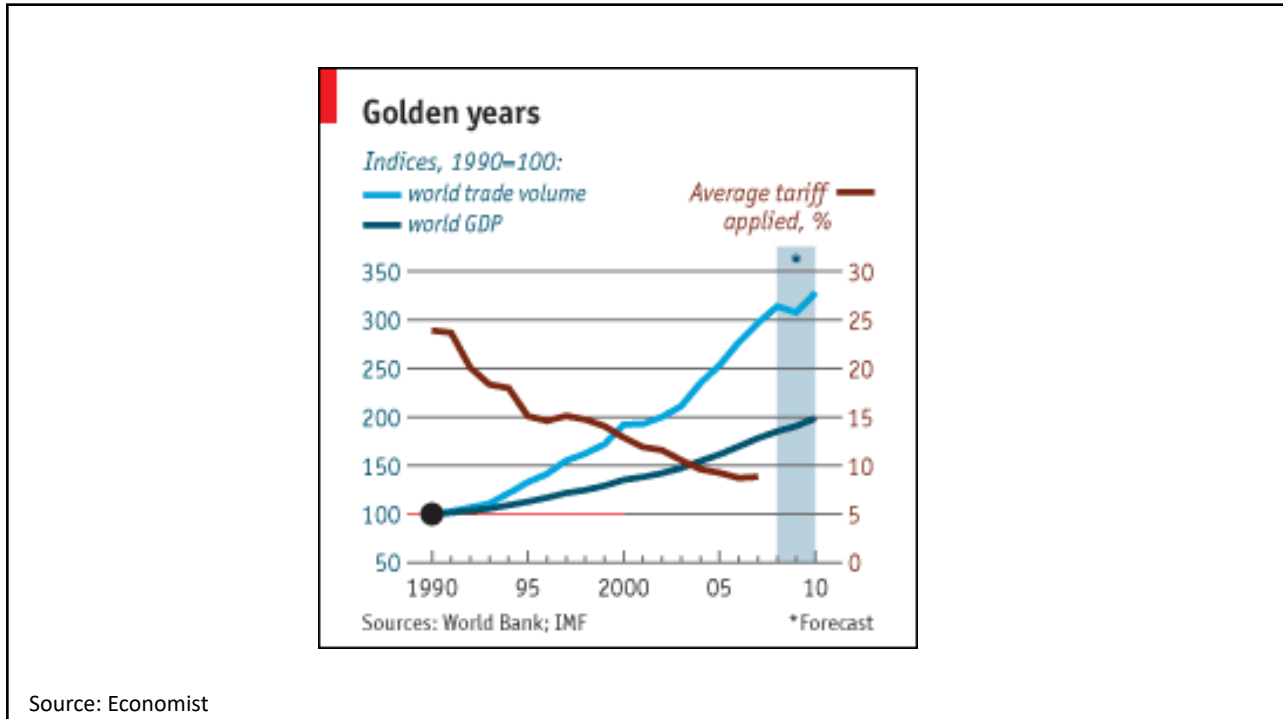


Tariff Reductions

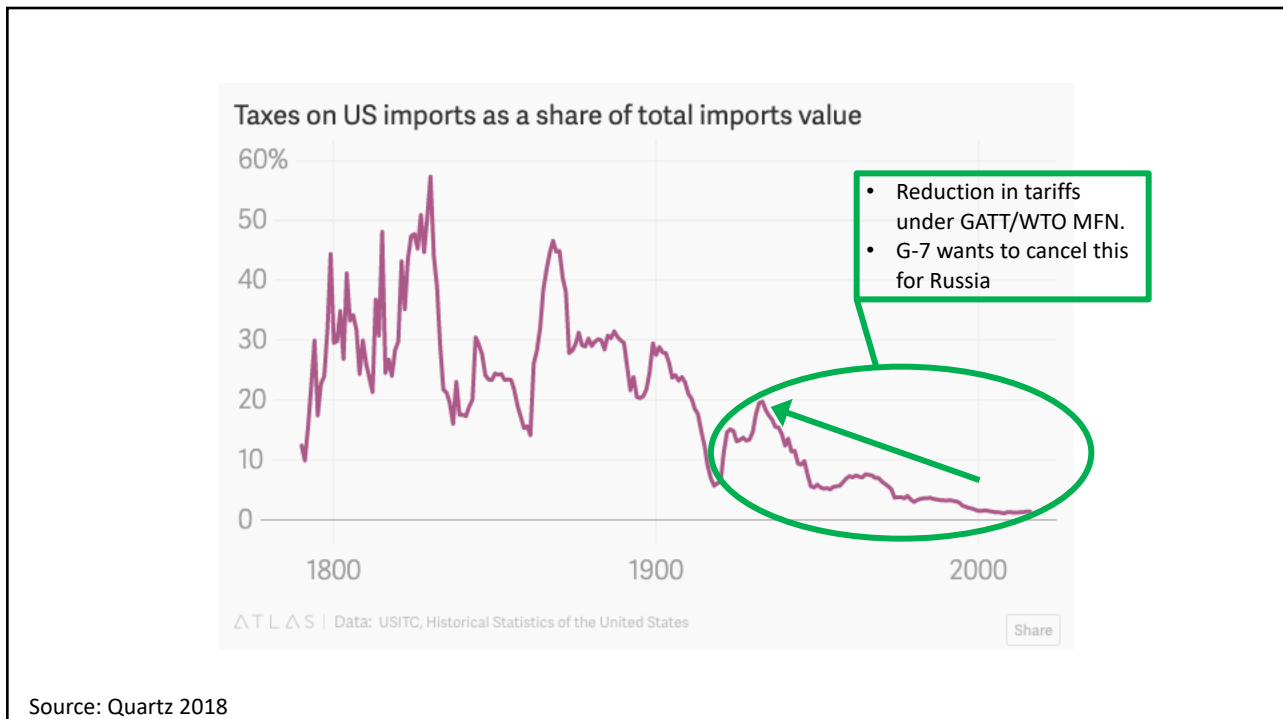


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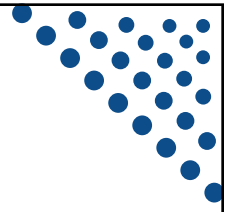
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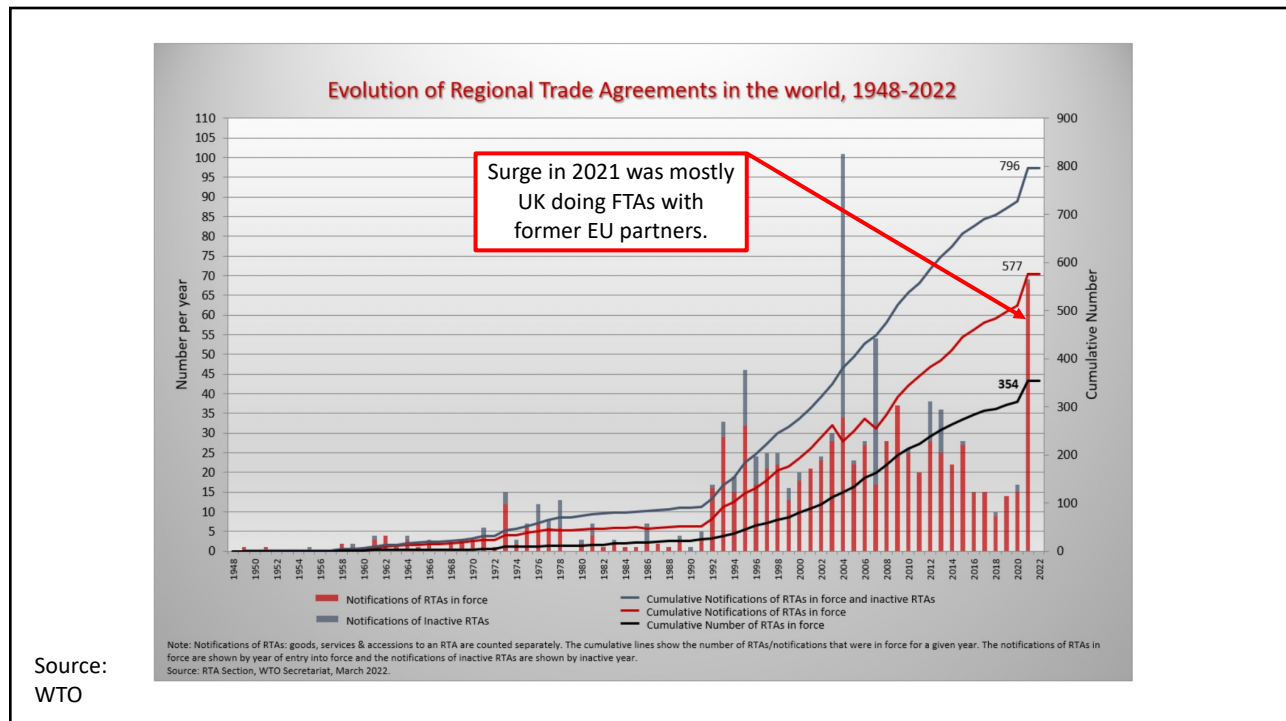
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Trade Agreements



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European Union



Source: Europa.eu

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NAFTA (now USMCA)



Download from Dreamstime.com

2848065 Jonyfigueroa | Dreamstime.com

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RCEP
=
**Regional
Comprehensive
Economic
Partnership**



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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, if time]**

- 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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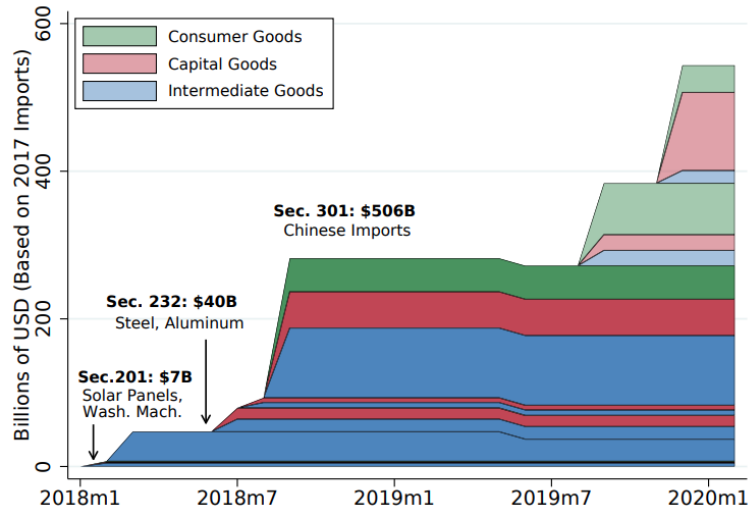
Trump's Tariffs and Trade War



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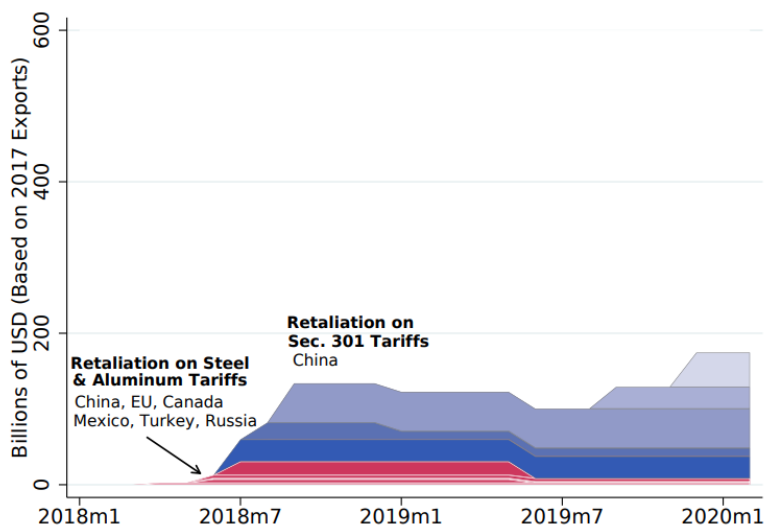
Figure B1: Composition of New U.S. Import Tariffs: 2018-2019



Source:
Flaan &
Pierce
2020

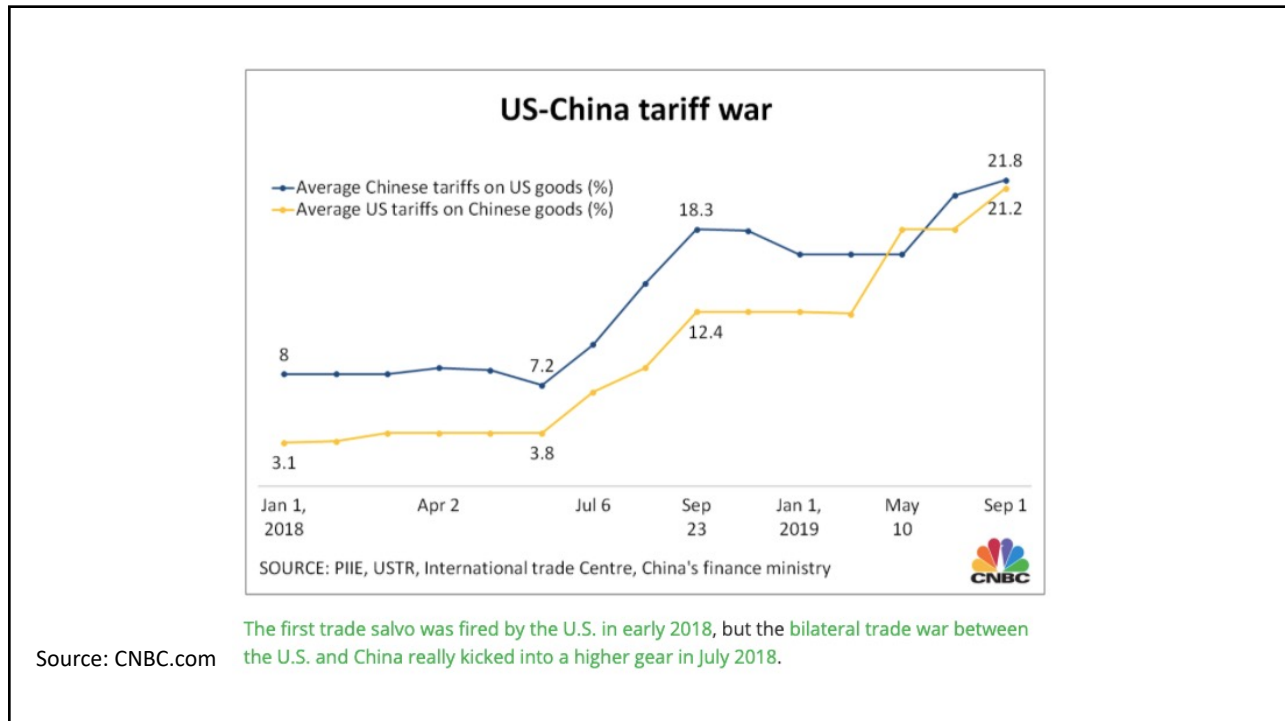
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Figure 3: Timeline of Retaliatory Tariffs on U.S. Exports: 2018-2019

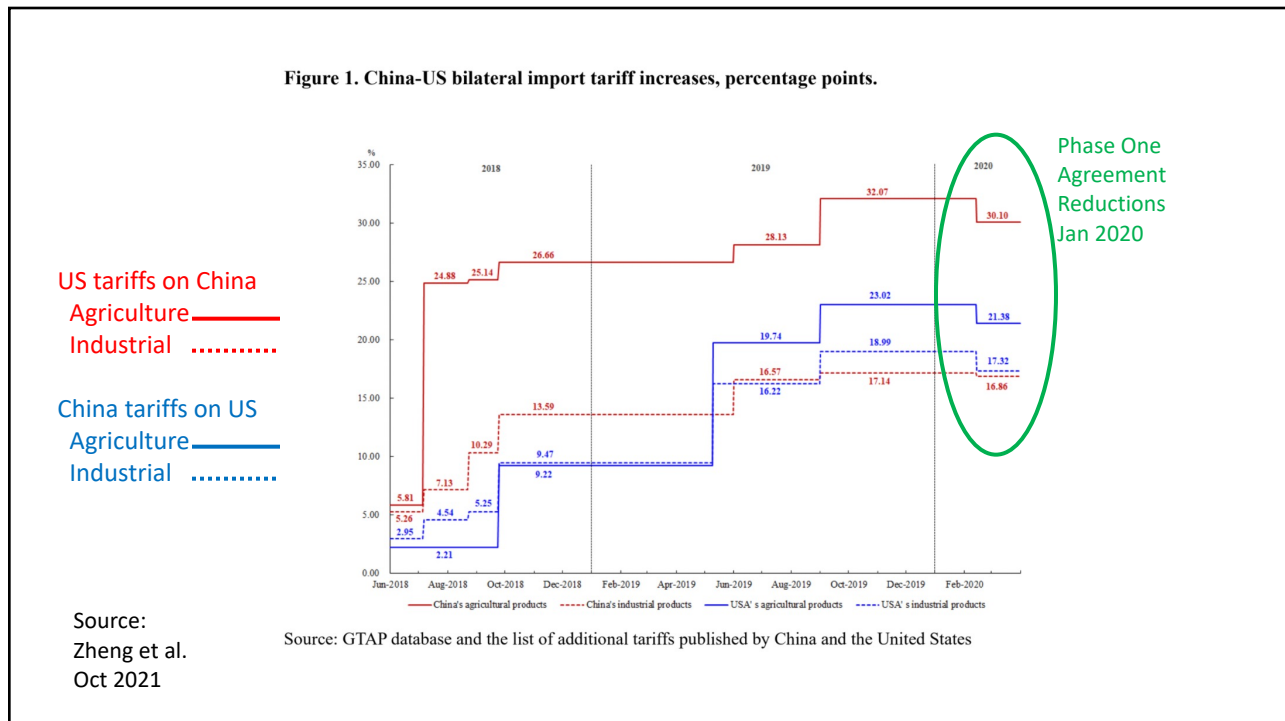


Source:
Flaan &
Pierce
2020


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Effects of Tariffs


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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 as large as the U.S.
 - Example: Trump's tariffs caused US prices to rise, with hardly any perceptible fall in prices abroad.

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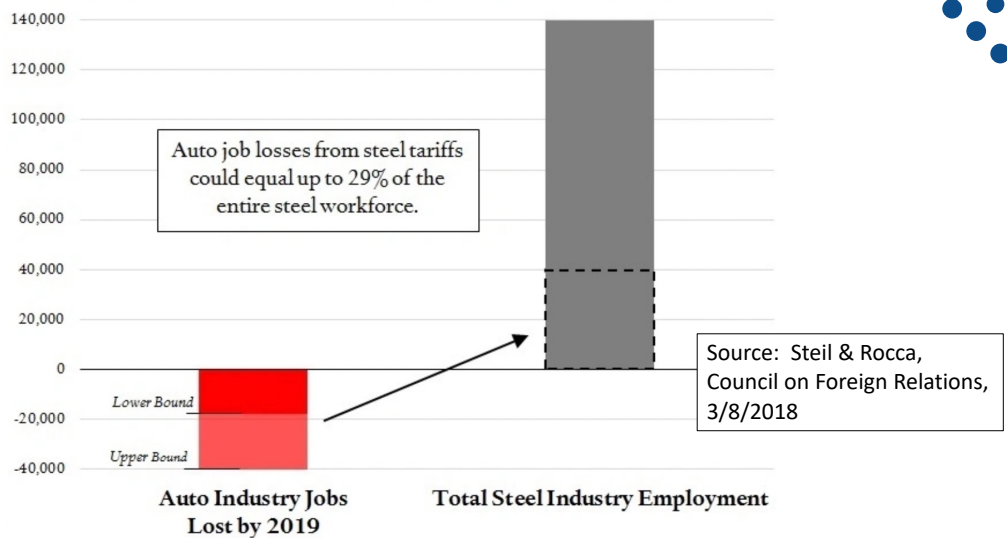
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Effects of a tariff

- **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
 - o Including producers that use the higher-priced goods as inputs
 - Their prices also rise, hurting their buyers
 - Employment changes:
 - o Increase in the protected industry
 - o Decrease in industries that use the protected product as inputs
 - Example: Trump's 25% tariff on steel
 - o Helped US steel firms and their workers
 - o Hurt US auto firms and workers
 - and many other industries that use steel

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U.S. Auto Jobs Jeopardized by Trump's Steel Tariffs



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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)

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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
 - Some are potentially valid, but better policies exist
 - See the list in my Glossary of International Economics

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Arguments for tariffs

Arguments for Protection

<p><u>Balance of payments</u></p> <p><u>Cultural</u></p> <p><u>Decreasing cost</u></p> <p><u>Domestic distortions</u></p> <p><u>Employment</u></p> <p><u>Environmental protection</u></p> <p><u>Externalities</u></p> <p><u>Fairness</u></p> <p><u>Foreign investment</u></p> <p><u>Graham's</u></p> <p><u>Income redistribution</u></p> <p><u>Infant industry</u></p> <p><u>Labor standards</u></p>	<p><u>Monopoly</u></p> <p><u>National defense</u></p> <p><u>Noneconomic objectives</u></p> <p><u>Optimal tariff</u></p> <p><u>Patriotism</u></p> <p><u>Pauper labor</u></p> <p><u>Revenue</u></p> <p><u>Second-best</u></p> <p><u>Self-sufficiency</u></p> <p><u>Strategic industry</u></p> <p><u>Strategic trade policy</u></p> <p><u>Sunset industry</u></p> <p><u>Terms of trade</u></p>
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Government Revenue

Distribution

Infant Industry

Source: Deardorffs' *Glossary of International Economics*

National security

Strategic trade policy

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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
 - **Lower tariffs and greater trade reduce the likelihood of war**

Skip to Conclusions

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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
 - o 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
 - o GATT (General Agreement on Tariffs and Trade) 1948
 - o WTO (World Trade Organization) 1995



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The Role of Trade Agreements

- **Trade Agreements (both WTO & FTAs)**

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



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The Role of Trade Agreements

- **WTO**

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



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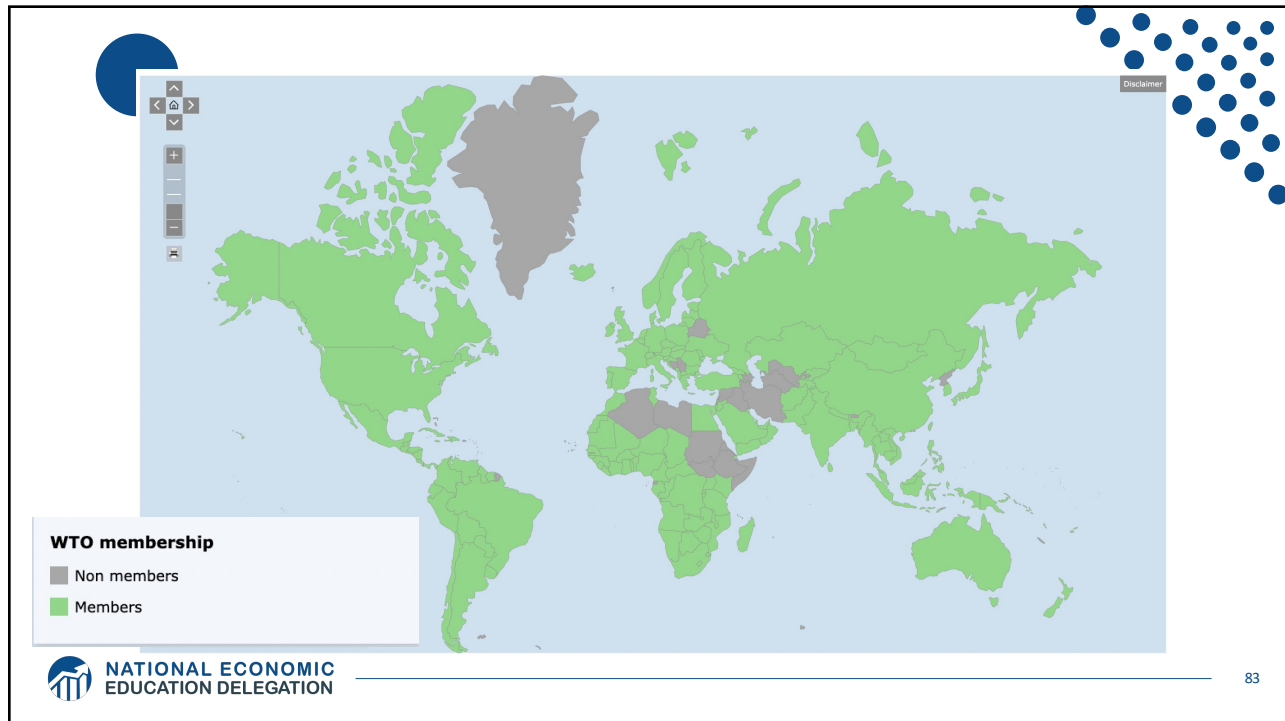
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The Role of Trade Agreements

- **The WTO has**
 - Three Parts:
 1. GATT (Still exists, as largest part of WTO)
 - limits tariffs
 - Permits exceptions (anti-dumping, etc.)
 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 (Don't discriminate among exporters)
 2. National Treatment (Don't discriminate against imports)

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The Role of Trade Agreements

• The WTO's Main Functions

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

The Role of Trade Agreements

• WTO Negotiation

- Ministerial Meetings
 - Held every ~2 years 1996-2017
 - Next #12 was delayed,
 - But is happening now, through tomorrow, in Geneva
 - Agreements
 - Multilateral
 - None on tariffs
 - A few on other measures (e.g., export subsidies in agriculture)
 - Plurilateral
 - Information technology
 - Telecoms
 - Financial services

The Role of Trade Agreements

• WTO Dispute Settlement

- There have been 612 cases initiated since 1995 (as of 6/15/22)
- About 90% have been decided in favor of the complainant, both by US (132) and against US (168)
- The mechanism has been unable to decide cases since December 10, 2019 when
 - o President Trump blocked appointments to Appellate Body
 - o President Biden has not changed this



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Globalization's Future?



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Globalization's Future?

- **Will trade, travel, etc. come back?**
 - Yes, but only partly.
 - They've been hit hard by financial crisis, trade war, pandemic, and now war
- **Will attitudes change?**
 - Yes.
 - Firm's will try to limit exposure ("just in case" instead of "just in time")
 - Consumers will learn to live differently
 - Reported July 20: Biden administration wants "friend-shoring." No mention yet of policies.
- **Will economists' views of globalization change?**
 - I think so.
 - o We still think globalization is good overall,
 - o But we're learning that it needs to include
 - Reduced reliance on single sources
 - Greater protections for those who are hurt.



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Autonomous Vehicles: Jon Haveman



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Thank you!

Any Questions?

www.NEEDelegation.org

Alan Deardorff
alandear@umich.edu

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