



Osher Lifelong Learning Institute, Winter 2023 **Contemporary Economic Policy**

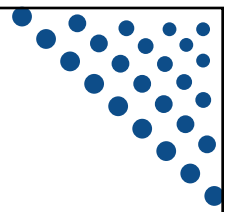
University of Rhode Island
January-February, 2023

Host: Jon Haveman, Ph.D.
National Economic Education Delegation



Available **NEED** Topics Include:

- US Economy
- Healthcare Economics
- Climate Change
- Economic Inequality
- Economic Mobility
- Trade and Globalization
- Minimum Wages
- Immigration Economics
- Housing Policy
- Federal Budgets
- Federal Debt
- Black-White Wealth Gap
- Autonomous Vehicles
- Healthcare Economics



Course Outline

• Contemporary Economic Policy

- Week 1 (1/10): Economic Update (Geoffrey Woglom, Amherst College)
- Week 2 (1/17): Monetary Economics (Geoffrey Woglom)
- **Week 3 (1/24): Trade and Globalization (Alan Deardorff, Univ. of Michigan)**
- Week 4 (1/31): Trade Deficits and Exchange Rates (Alan Deardorff)
- Week 5 (2/7): Autonomous Vehicles (Jon Haveman, NEED)



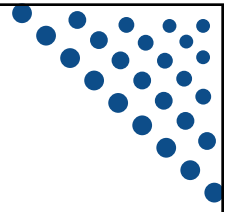
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Submitting Questions

- **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 University of Rhode Island
January 24, 2023



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Impact of Russia-Ukraine War

- **How Russia-Ukraine war impacts globalization**

- War itself disrupts trade, especially exports of
 - o Ukraine: wheat
 - o Russia: wheat, oil
- Economic sanctions by governments disrupt
 - o Financial linkages
 - o 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

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 frnd | 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

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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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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

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Halting investments

96 companies, including ...

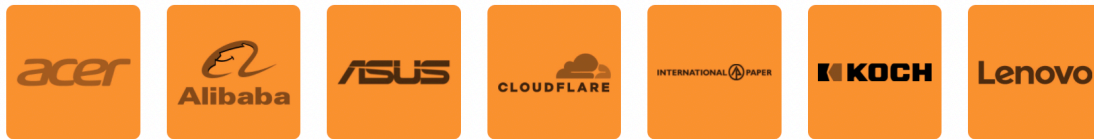


Source: New York Times, April 7, 2022

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Staying the course

162 companies, including ...

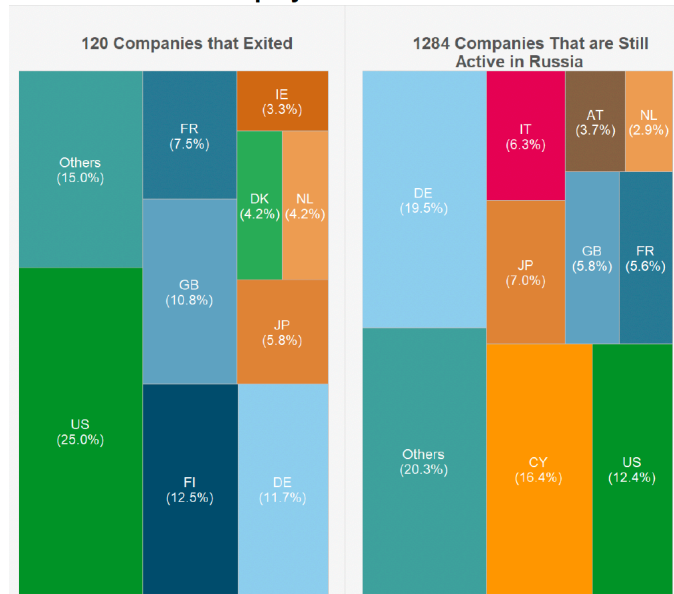


Source: New York Times, April 7, 2022

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Country of origin of EU and G7 Companies with an Equity Stake in Russia

But...
Recent study reports:
“Less Than Nine Percent of Western Firms Have Divested from Russia”



Source: Evenett and Pisani, December 20, 2022

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Effect of Sanctions

- **Too soon to know fully**
 - Will they stop Russia?
 - Clearly no
 - Sanctions in the past have only sometimes worked
 - Will they reduce trade?
 - They did
 - But Russia's role in trade is not large in most products
 - 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)**



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What Globalizations Is

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



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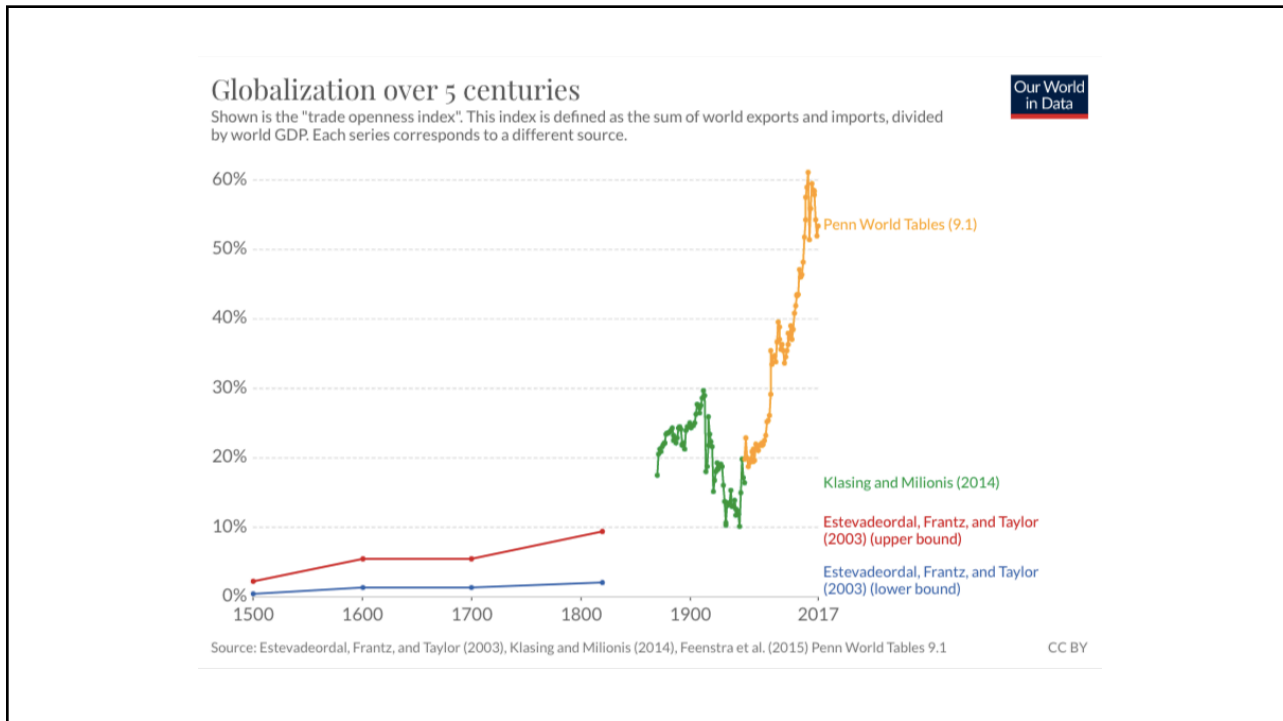
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Trade

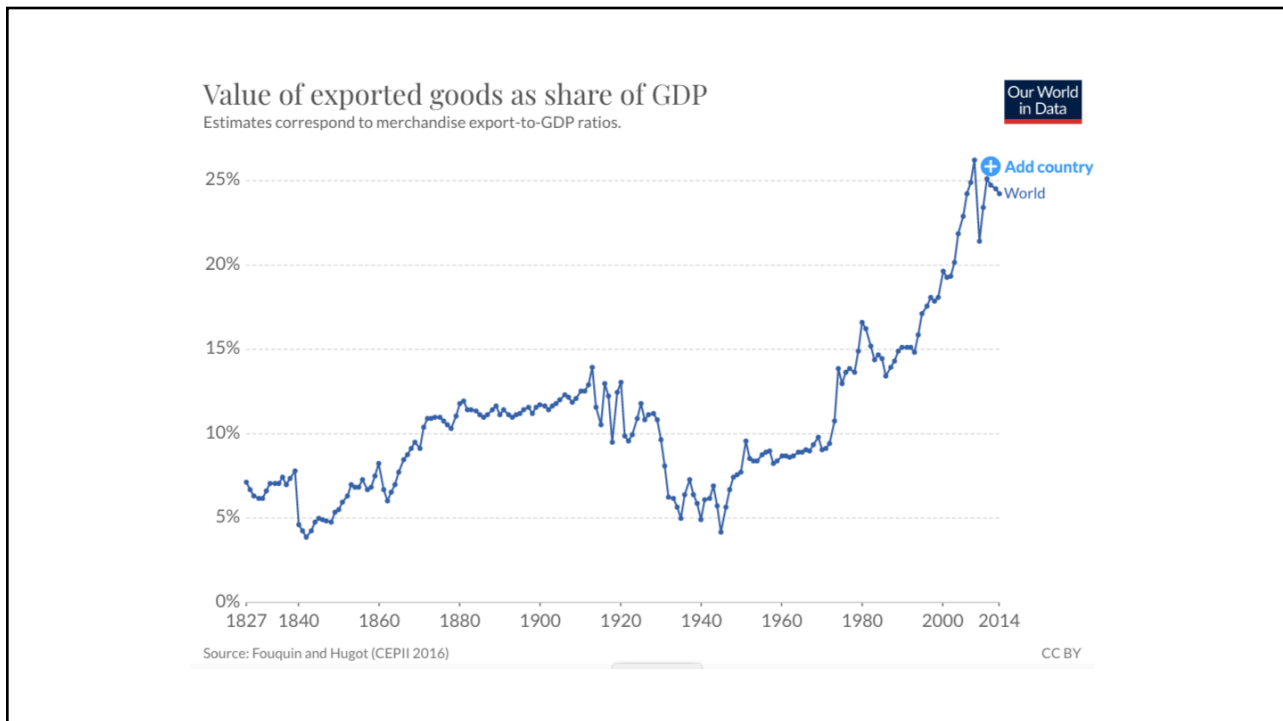


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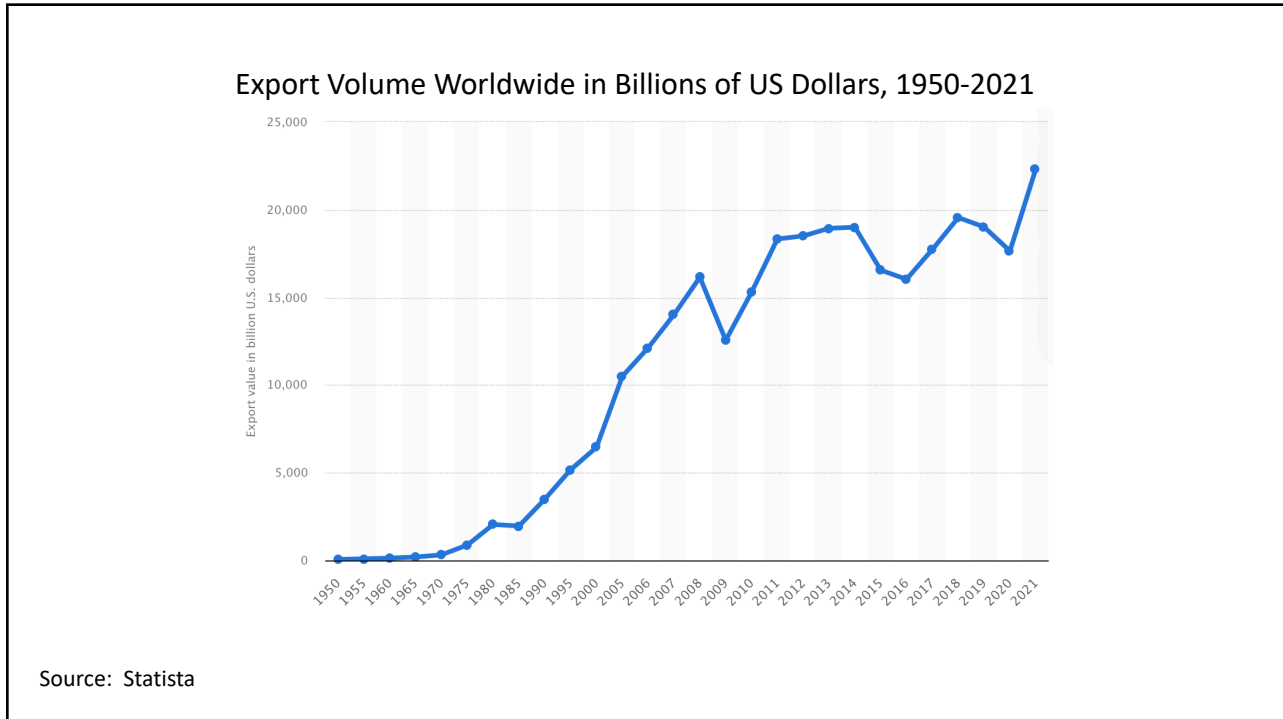
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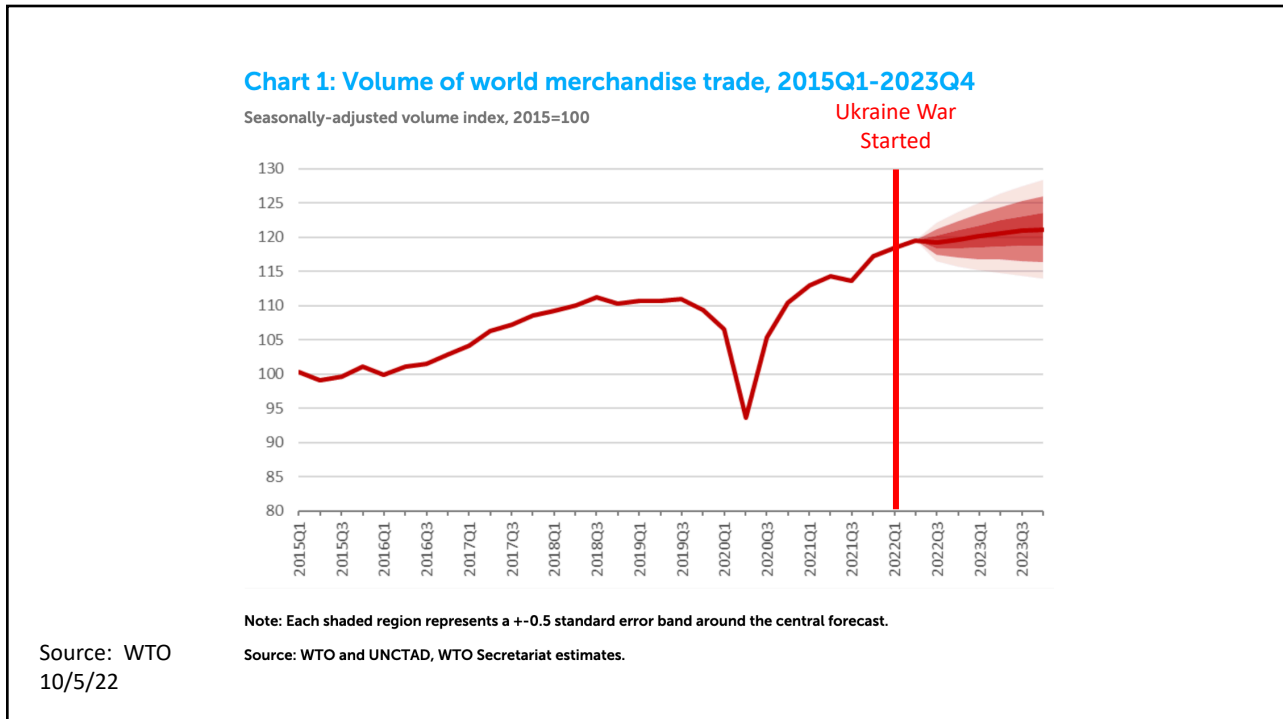
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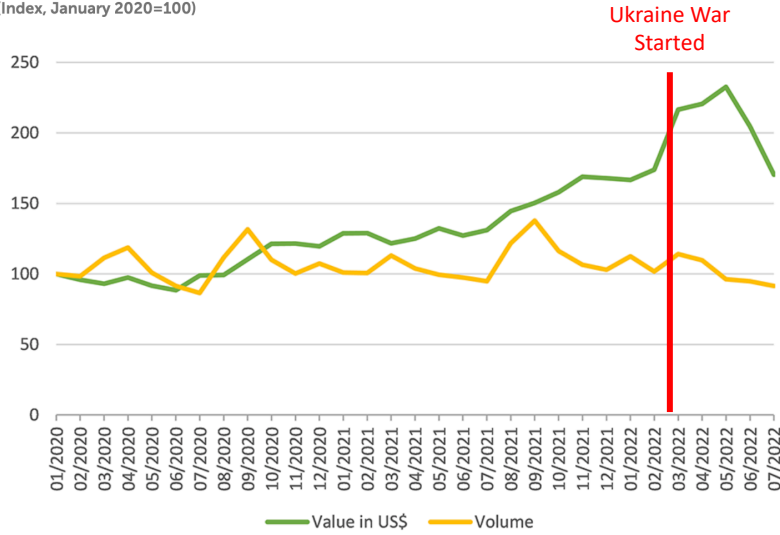
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Chart 3: Estimated value and volume of world trade in wheat, January 2020 - July 2022

(Index, January 2020=100)

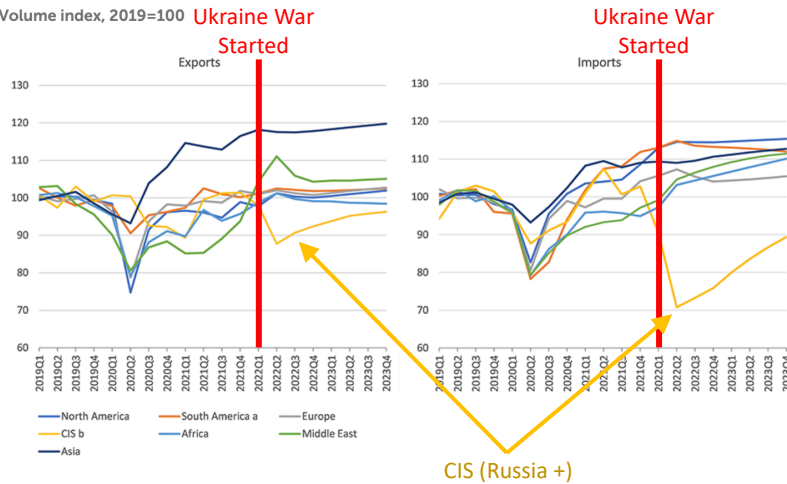


Source: WTO
10/5/22

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Chart 4: Merchandise exports and imports by region, 2019Q1-2023Q4

Volume index, 2019=100



a. Refers to South and Central America and the Caribbean.

b. Refers to the Commonwealth of Independent States, including certain associate and former member States.

Source: WTO and UNCTAD.

Source: WTO
10/5/22

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Global Value Chains



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Effects on Economies

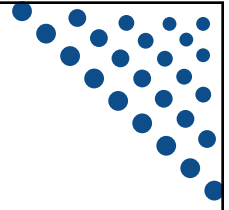
- **Supply Chains**
 - Globalization has created long and complex international supply chains



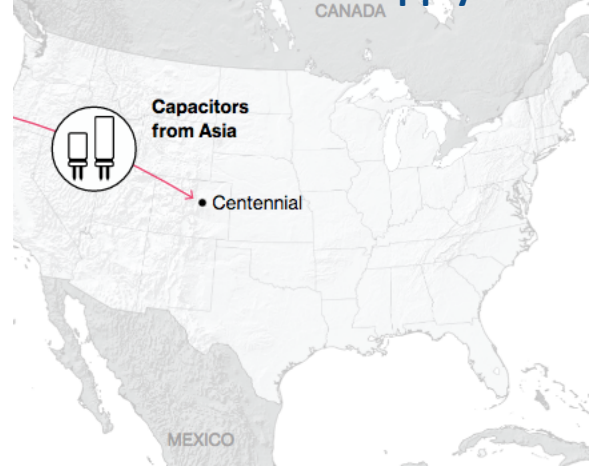
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NAFTA and the Auto Supply Chain

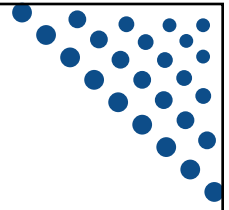


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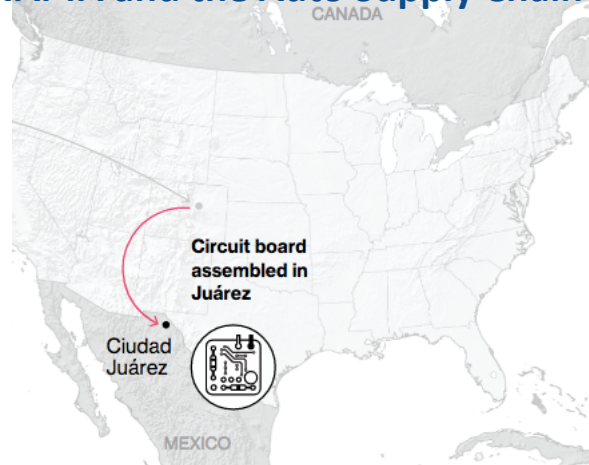
Black, Diamond, and Merrill, "One Tiny Widget's Dizzying Journey Shows Just How Critical Nafta Has Become," *Bloomberg*, February 2, 2017.

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NAFTA and the Auto Supply Chain

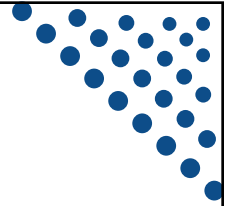


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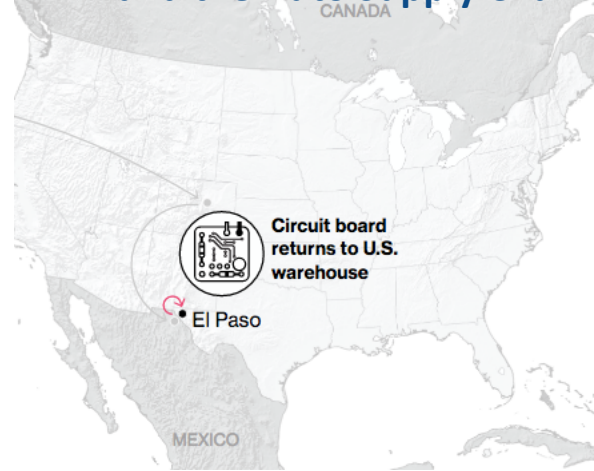
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NAFTA and the Auto Supply Chain

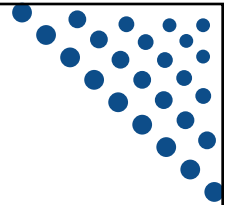


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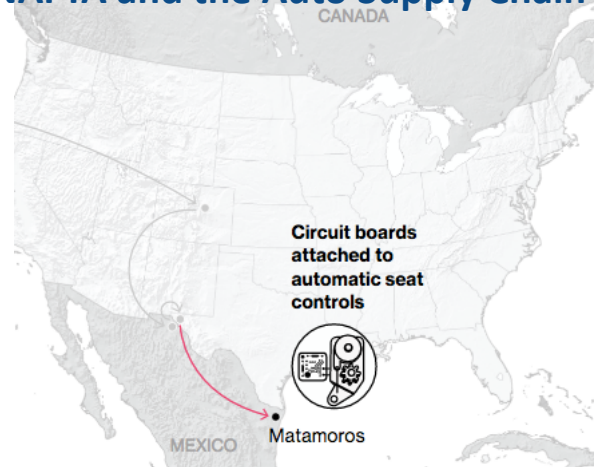
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NAFTA and the Auto Supply Chain

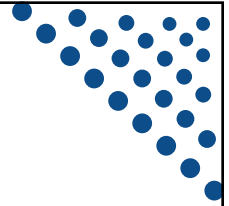


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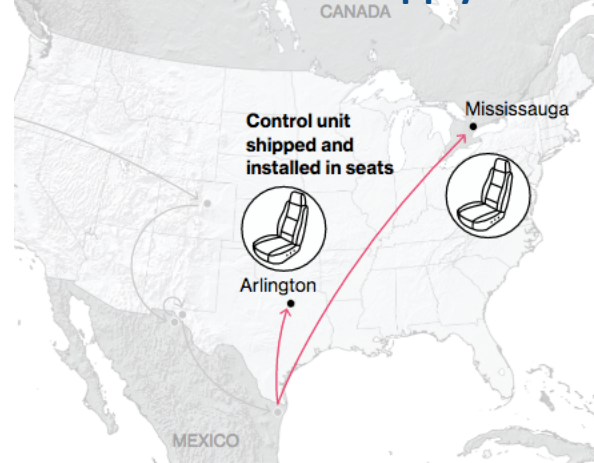
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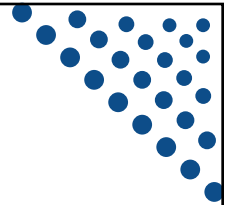


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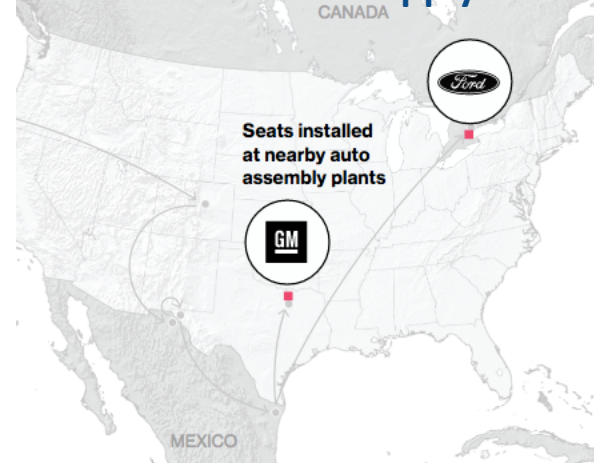
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NAFTA and the Auto Supply Chain



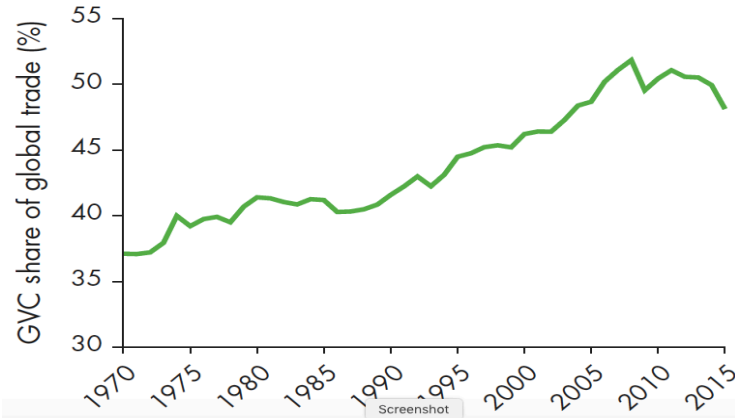
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Growth of Global Value Chains, 1970-2015

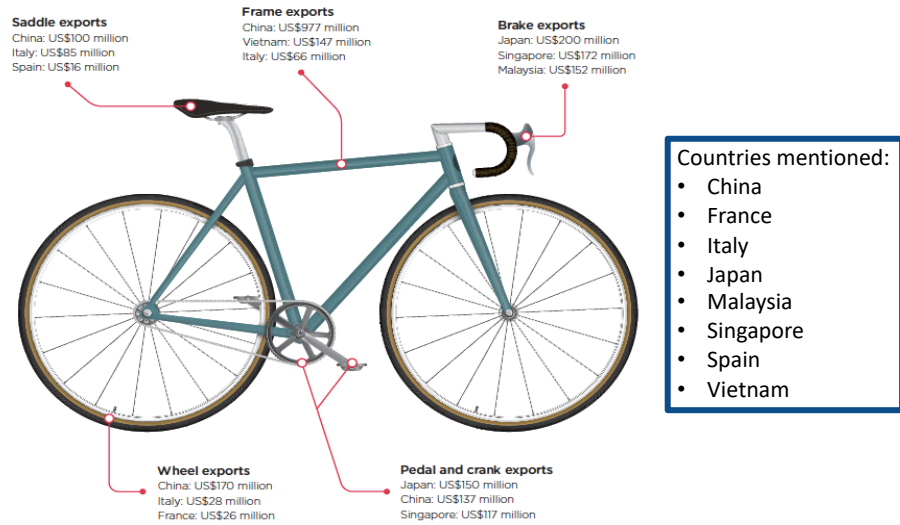
Figure 1.2 GVC trade grew rapidly in the 1990s but stagnated after the 2008 global financial crisis



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

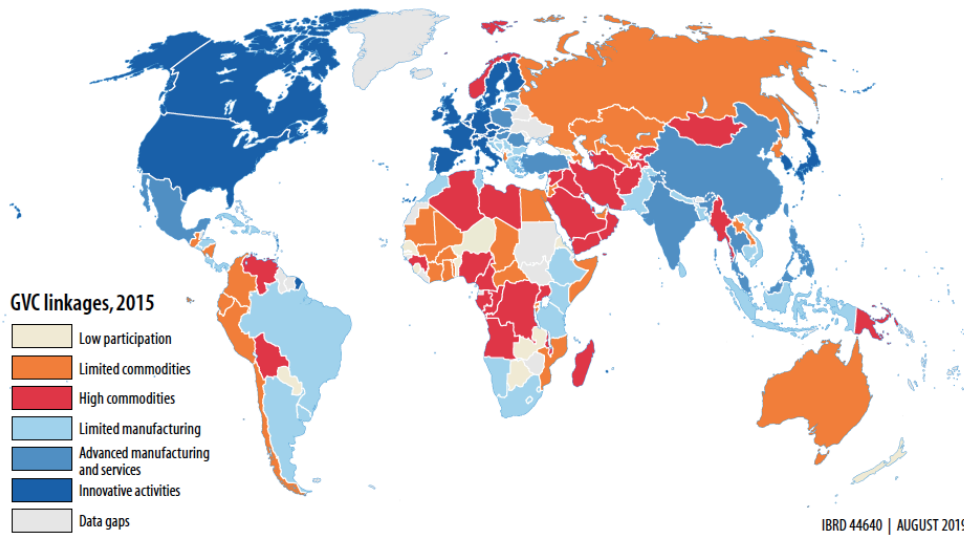
• Example: The iPhone assembled in China from parts:

| 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

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



IBRD 44640 | AUGUST 2019

Source: World Bank

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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

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**

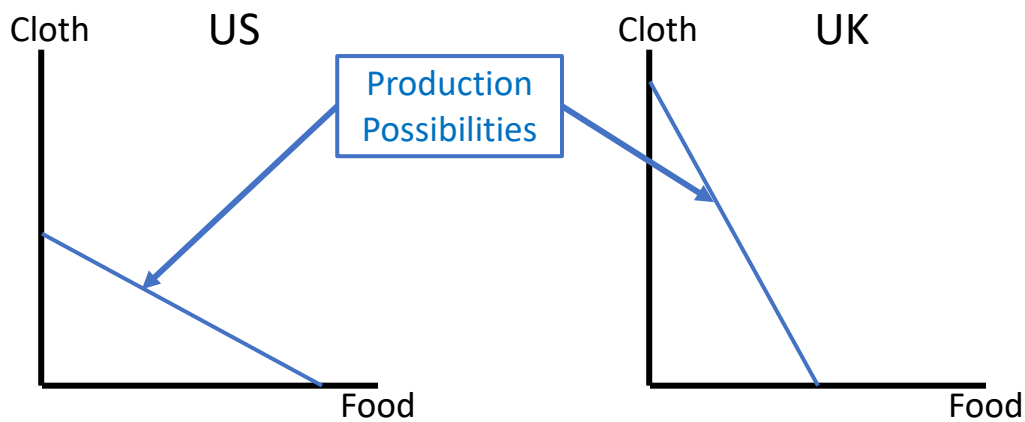


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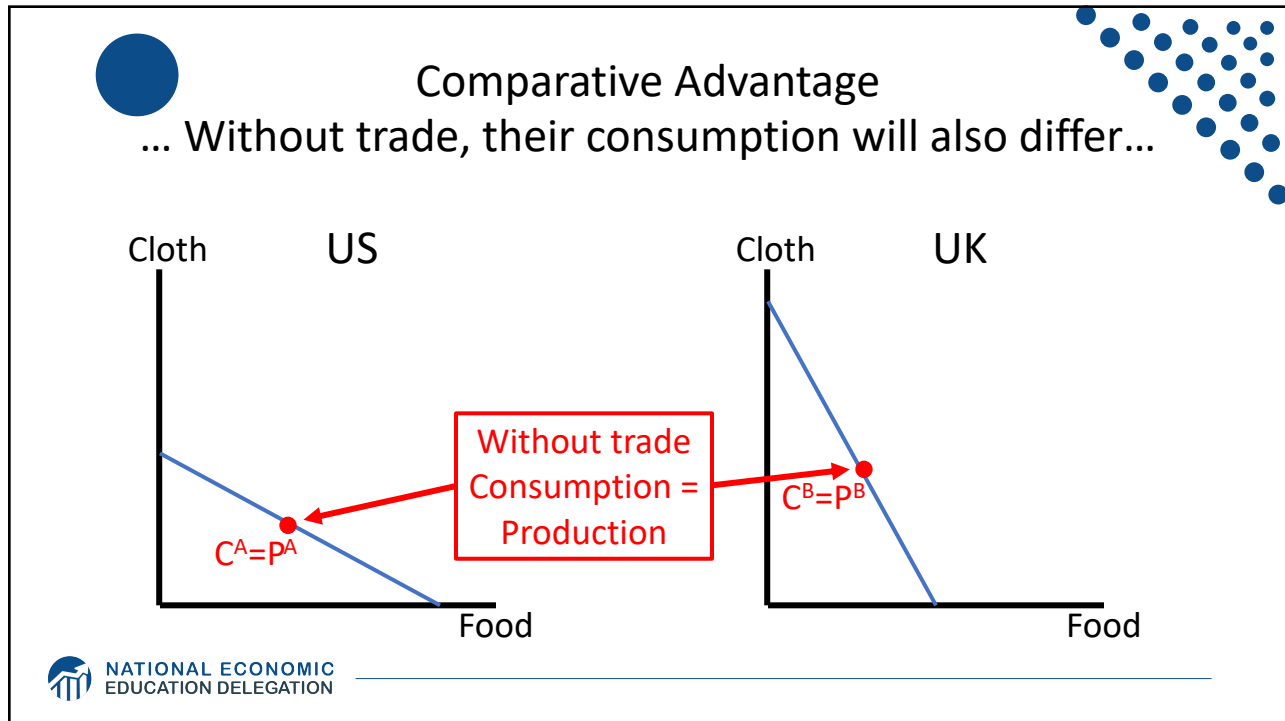


Comparative Advantage If US & UK differ in what they can produce...

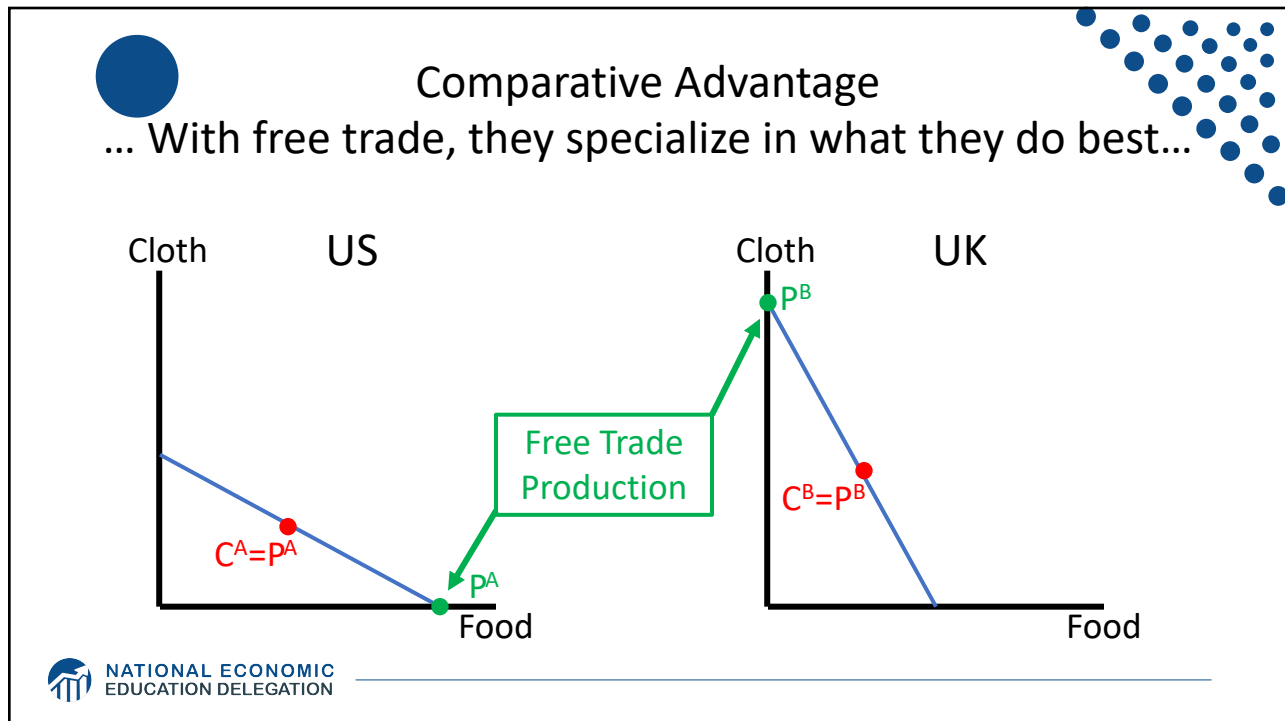


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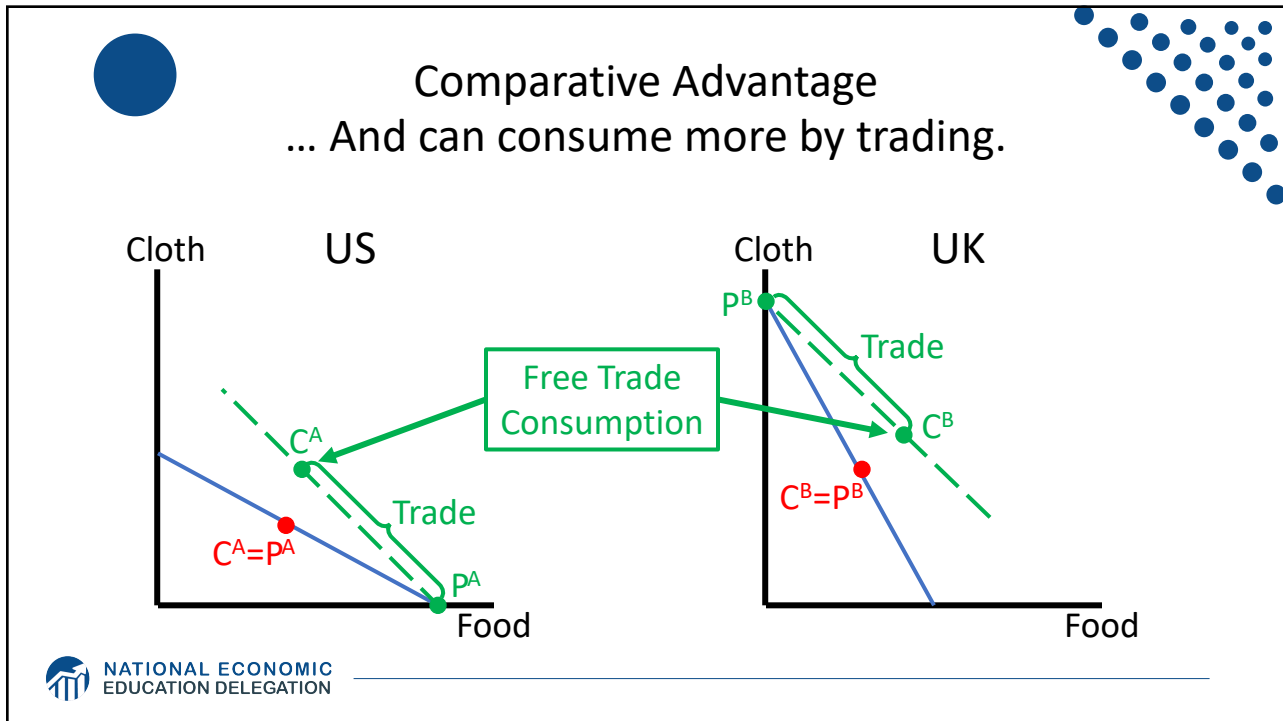
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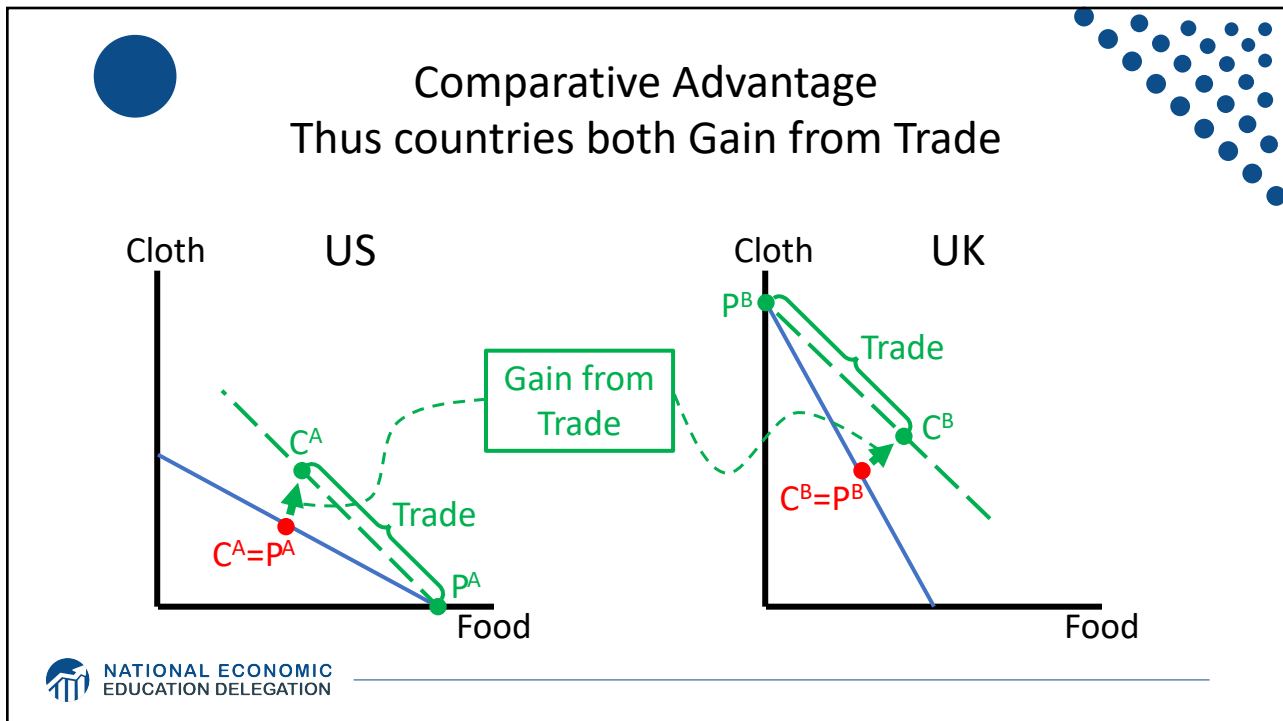
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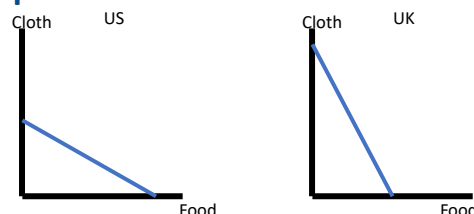
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Sources of Comparative Advantage

- Differences in countries' production possibilities



- These are due to differences in

- Resources
 - o Labor
 - o Land
 - o Capital
- Technologies (know-how)



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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.)
 - o 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
 - o (However, the gains from trade then accrue to countries including their mobile-factor owners.)



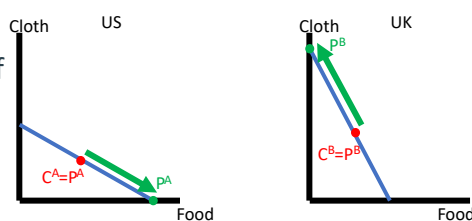
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Generality of Comparative Advantage

• 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)

Costs of Trade

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



Pause

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



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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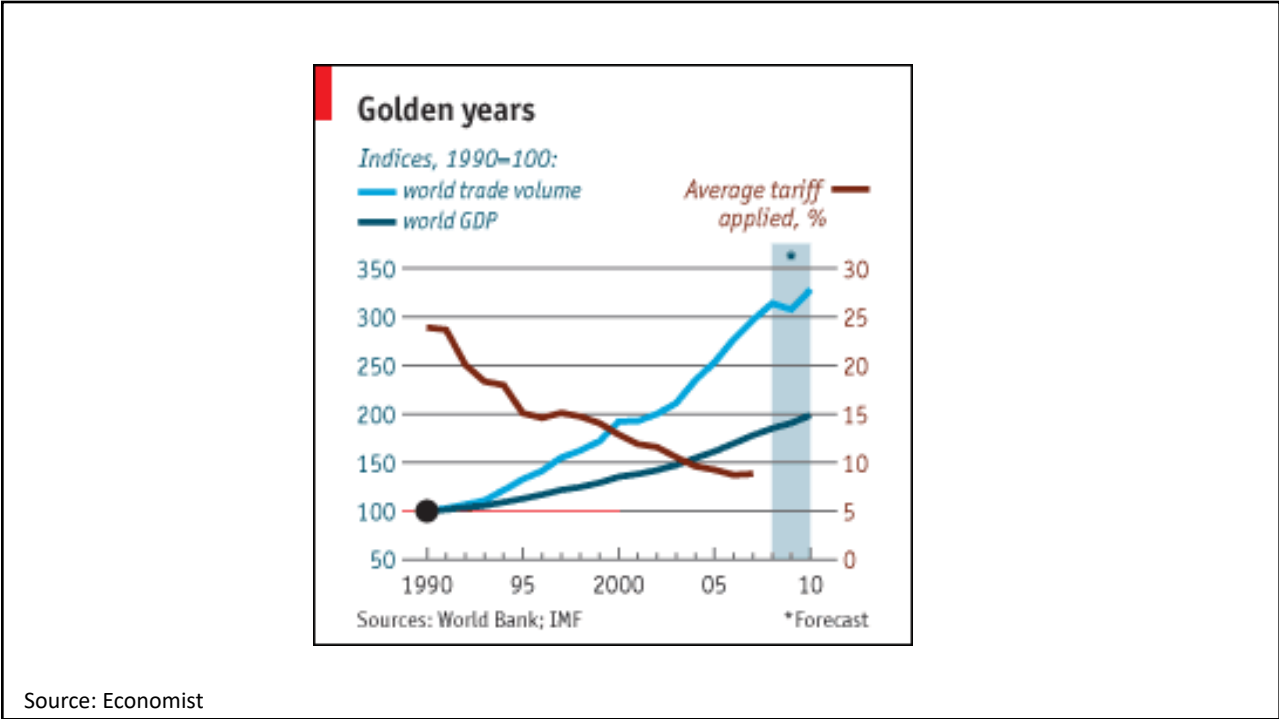
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Tariff Reductions

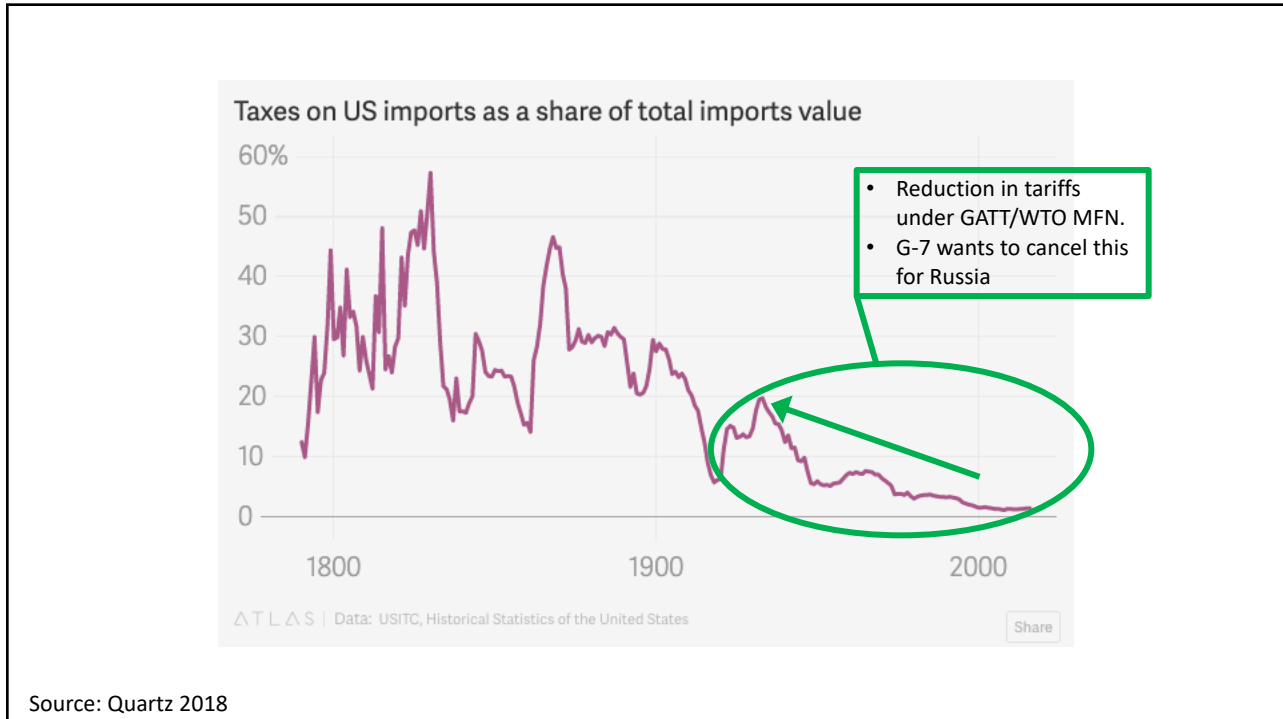
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Source: Economist

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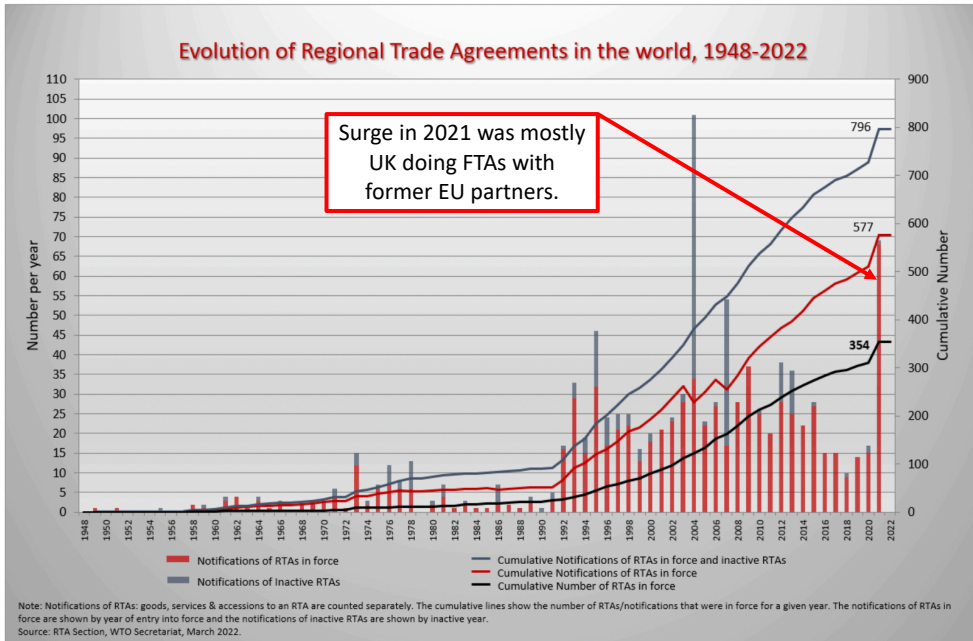


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Trade Agreements

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Surge in 2021 was mostly UK doing FTAs with former EU partners.

Source: WTO

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European Union



Source: Europa.eu

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NAFTA (now USMCA)

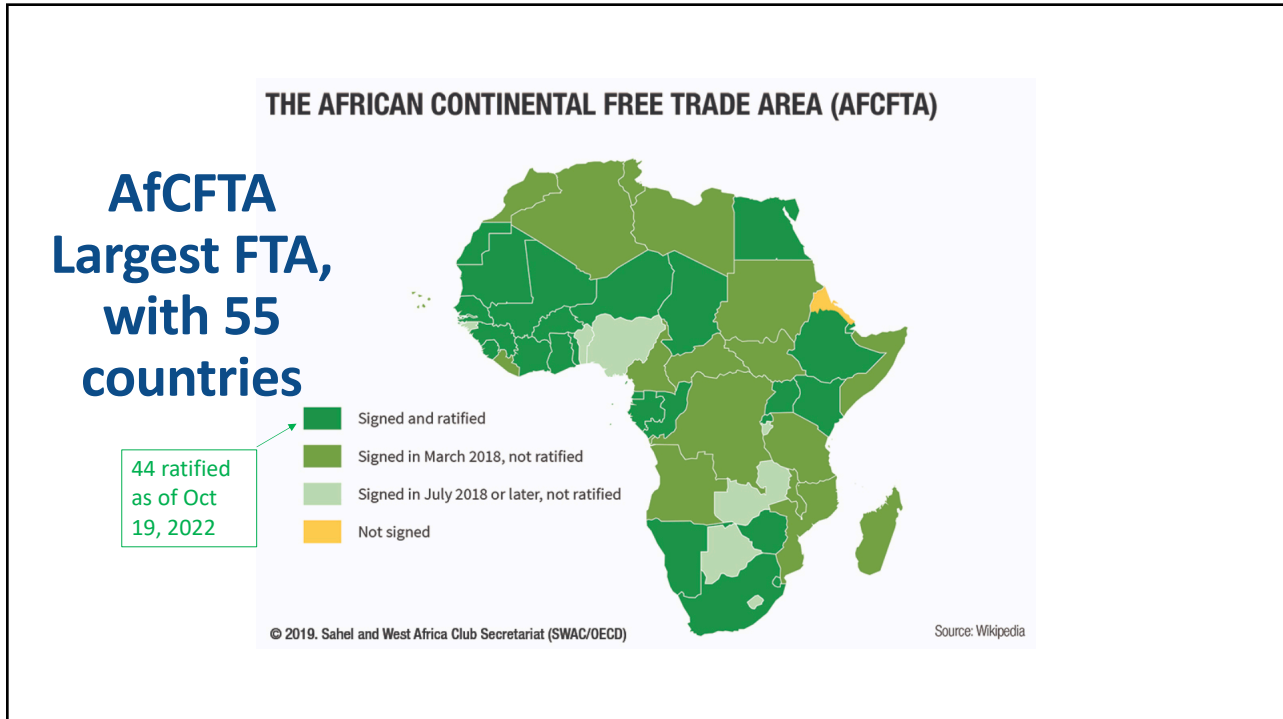


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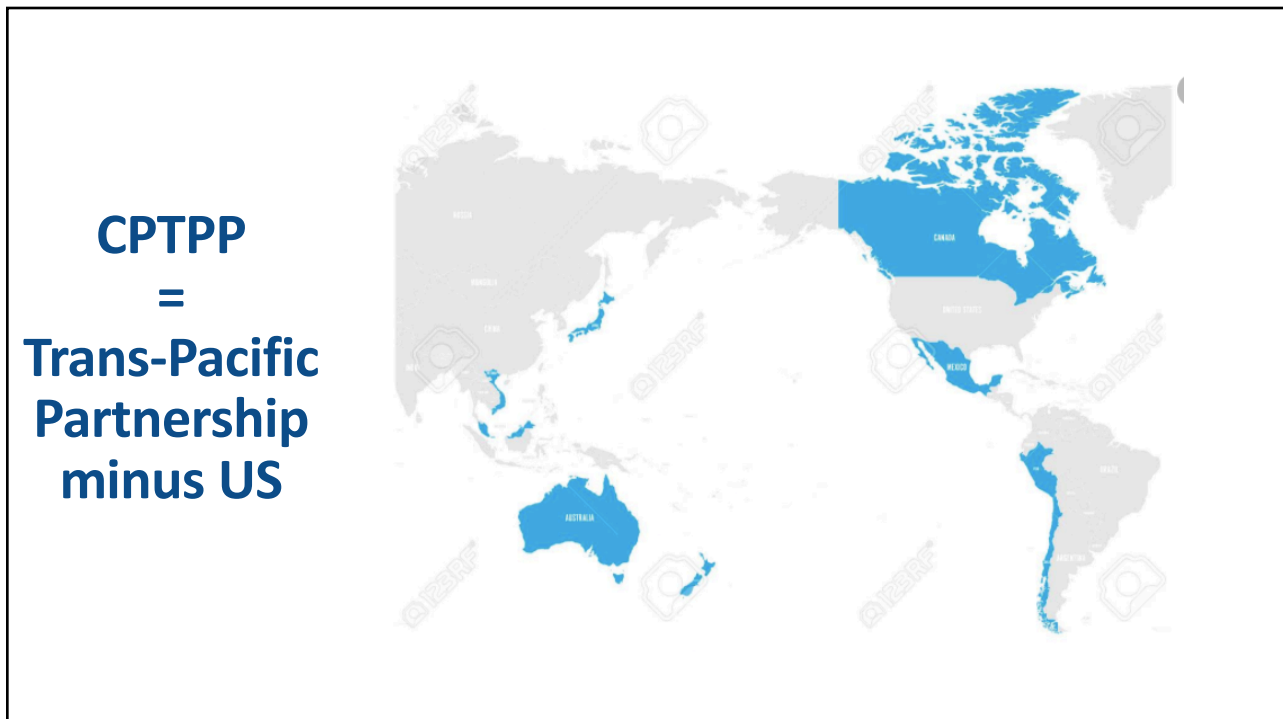
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RCEP
=
**Regional
Comprehensive
Economic
Partnership**



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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
 - Reducing trade barriers
 - 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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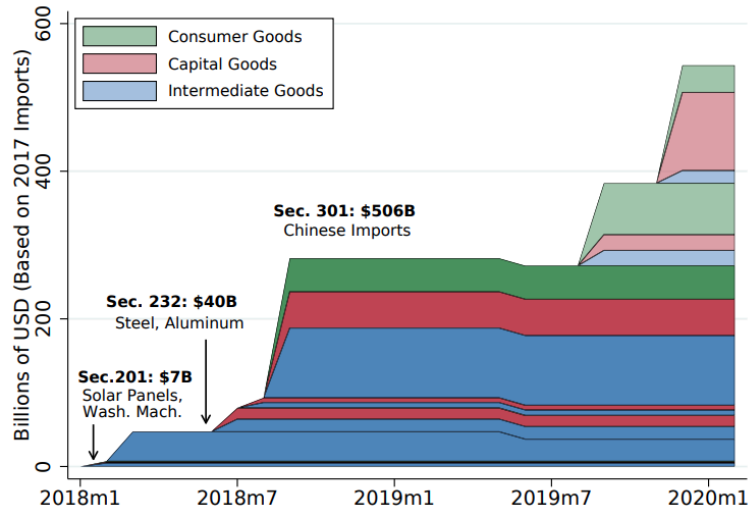
Trump's Tariffs and Trade War



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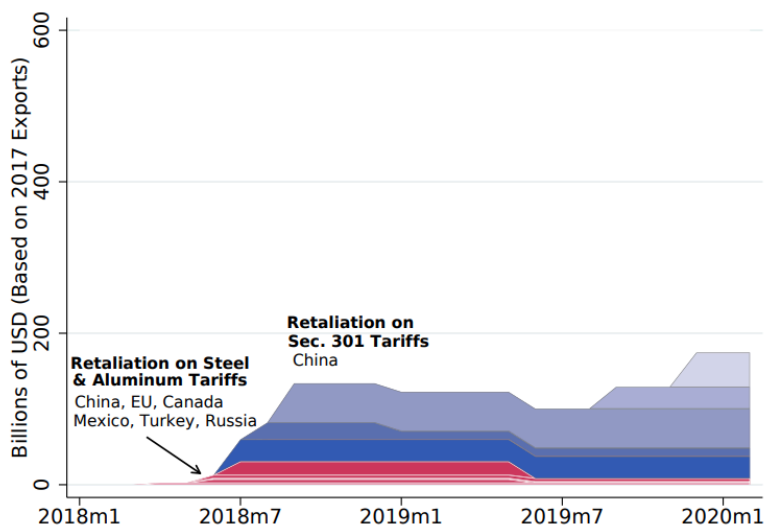
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Figure B1: Composition of New U.S. Import Tariffs: 2018-2019

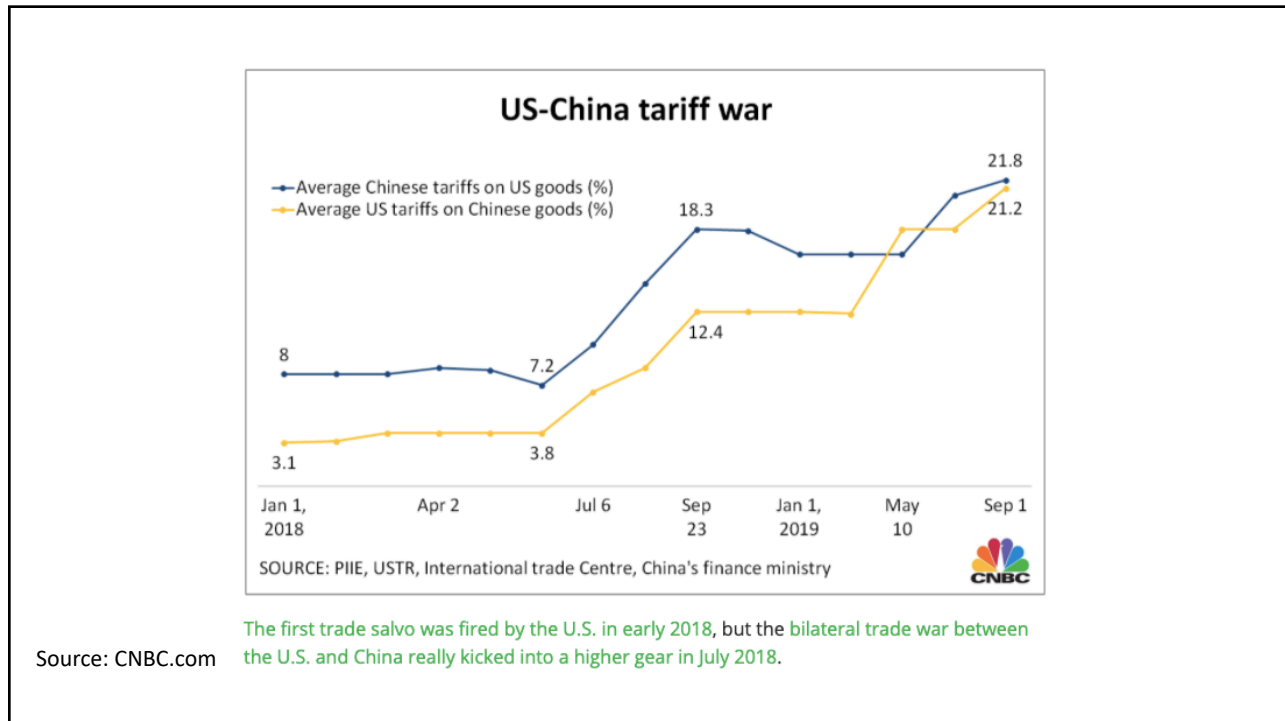


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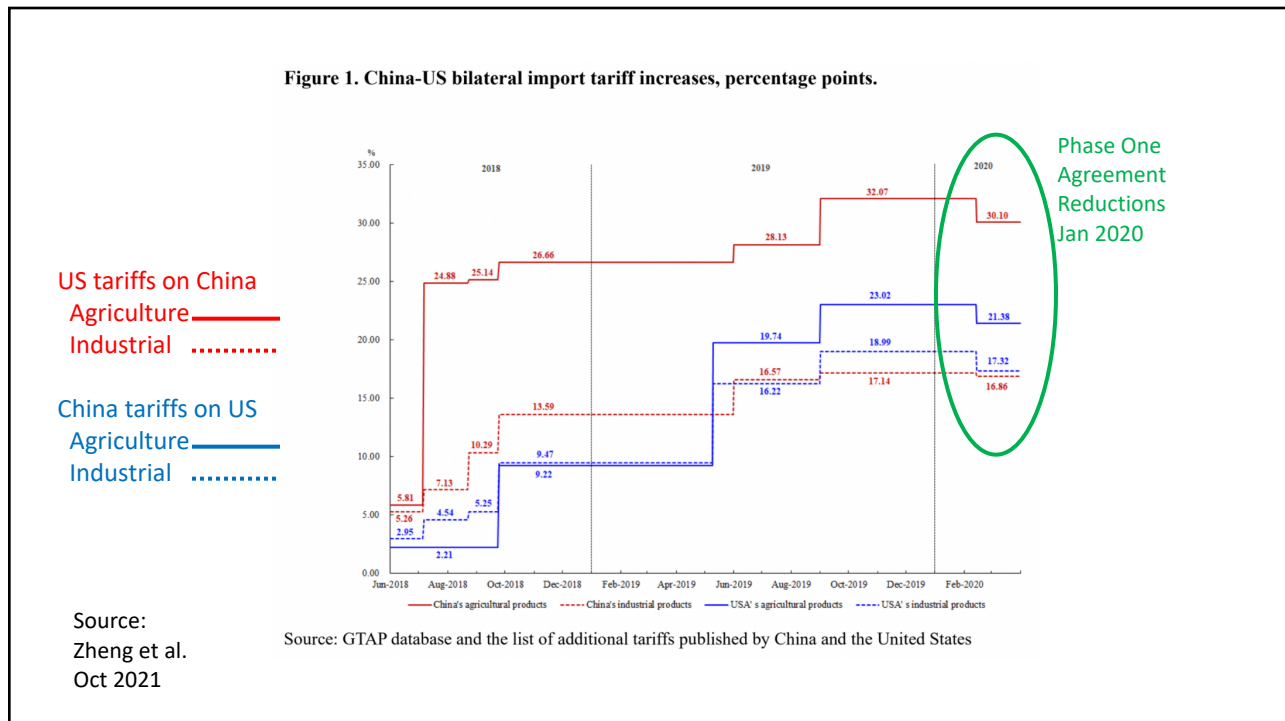
Figure 3: Timeline of Retaliatory Tariffs on U.S. Exports: 2018-2019



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Effects of Tariffs




Effects of a tariff

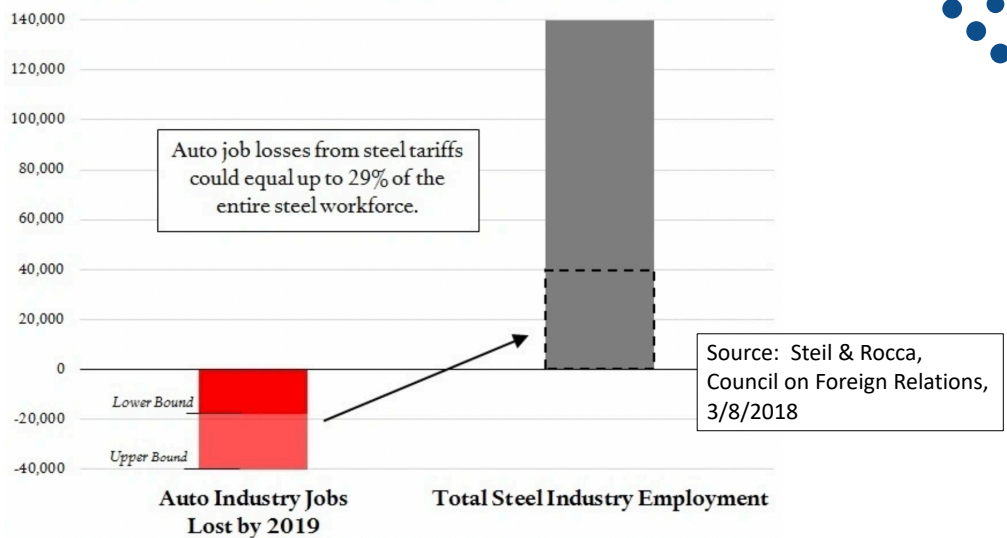
- **A tariff is a tax on imports. It causes**
 - A rise in the price of the imported good in the importing country
 - A fall in the price of the imported good in the exporting country
 - The quantity imported to fall
 - The revenue of the tariff-levying government to rise
- **Almost always: the rise 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 as large as the 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 the protected product as inputs
 - Example: Trump's 25% tariff on steel
 - Helped US steel firms and their workers
 - 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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- “Nationally, steel and aluminum tariffs resulted in at least 75,000 job losses in metal-using industries by the end of last year [2019],
 - according to an analysis by Lydia Cox, a Ph.D. candidate in economics at Harvard University, and Kadee Russ, an economics professor at the University of California, Davis.”

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Effects of a tariff

- **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)
 - Sellers shift to export to other countries that pay less
 - Both lose a little

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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

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

Government Revenue

Distribution

Infant Industry

National security

Strategic trade policy

Source: Deardorff's *Glossary of International Economics*

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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**



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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
 - 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



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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

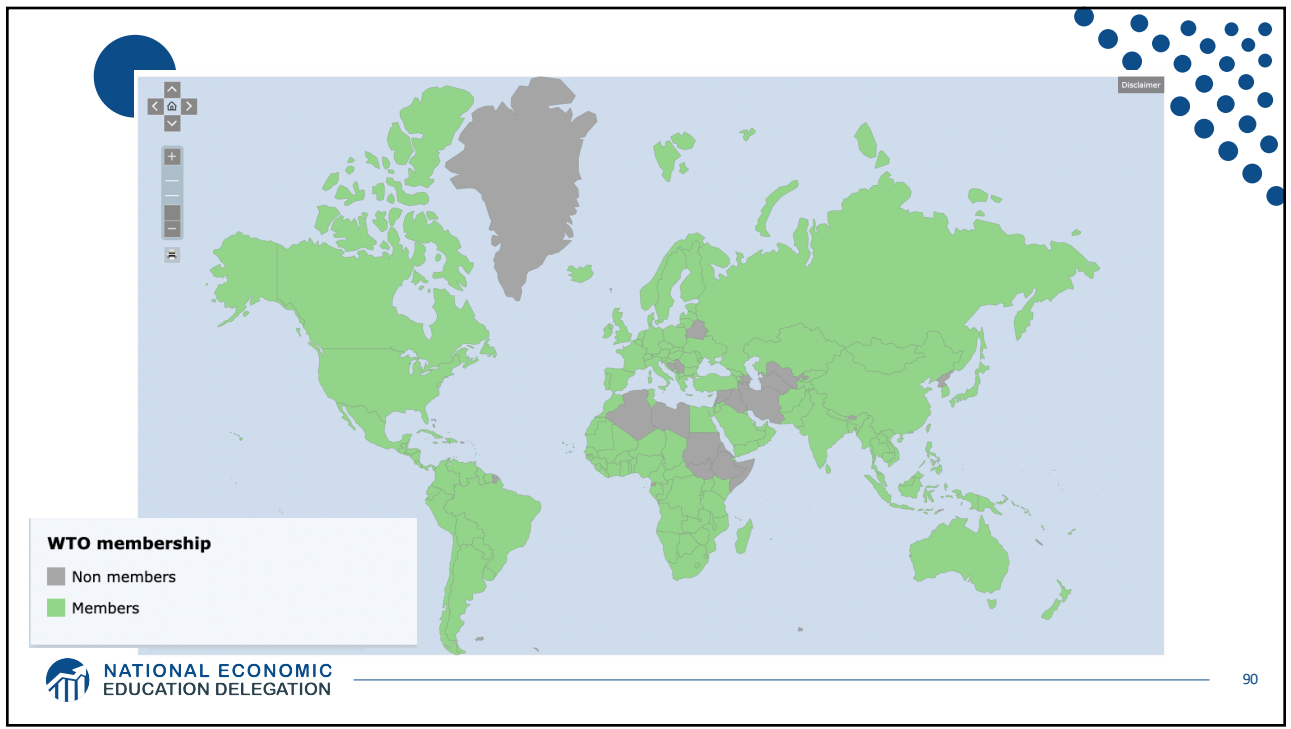


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The Role of Trade Agreements

• 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 has not)
- Removal of other barriers

- Dispute settlement

- Countries bring cases against others
- WTO "panels" and "Appellate Body" decide



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The Role of Trade Agreements

• WTO Negotiation

- Ministerial Meetings
 - Held every ~2 years 1996-2017
 - Most recent, #12, was delayed,
 - But happened June 12-17, 2022, in Geneva
 - Didn't do much: Ended subsidies to illegal fishing
 - Next, #13, will be in 2024, in United Arab Emirates



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The Role of Trade Agreements

• WTO Negotiation

- Agreements
 - Multilateral (all members)
 - None on tariffs
 - A few on other measures (e.g., export subsidies in agriculture)
 - Plurilateral (willing members)
 - Information technology
 - Telecoms
 - Financial services



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The Role of Trade Agreements

• WTO Dispute Settlement

- There have been 615 cases initiated since 1995 (as of 1/10/23)
- 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 may 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.



Next Week

Trade Deficits and Exchange Rates

Me





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Thank you!

Any Questions?

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