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ECON 3100

Course Substitution: Major/Minor Credit

DUE: June 24, 2024

Part I: Podcasts: Go to the website https://www.tradetalkspodcast.com and listen to the podcast on TradeTalks – Episode 181 “US China trade war fallout: This is what decoupling looks like” and Episode 180 The WTO is in trouble: Econ 101 to the rescue. Write a summary of these episodes – each review should be no longer than one page.

Summary of Episode 180:

The WTO is struggling after the failure of the Doha Round. Member nations are looking elsewhere to negotiate trade issues and agreements. The hosts discuss the start of the WTO and the economic principles it is founded upon, as well as its predecessor, the GATT. Bob Staiger explains that the goal of the WTO is not free trade but "for countries to internalize the externalities that they impose on each other". He explains that tariffs do not necessarily need to be zero. The hosts discuss an example of the EU and the US and agree that the WTO is helpful in making tariff decisions and negotiations and that the WTO is not about free trade but levels of market access between national economies.

They go on to discuss reciprocity and changes in tariffs with the goal to match changes in import volume to changes in export volume. They explain that when countries lower tariffs, they do so mainly because they expect the other countries to reciprocate in order to benefit from lower tariffs. Staiger discusses the property and liability rules as ways that countries can raise tariffs after agreeing to lower them.

Staiger and Brown then discuss how even small countries can hold market power and the ability to decide tariffs in certain industries. They talk about how the initial GATT negotiations were conducted with pen and paper, not tablets. It was a much longer process for each country to write out tariffs for certain industries and products with certain trading partners. The language barrier was also likely more difficult to navigate without the help of online translating services. They discuss the evidence of reciprocity and how nations who offer a low-ball tariff cut cannot except a large tariff cut in return.

Next, they talk about the trade war with China. China is a non-market economy, so they don't reciprocate market access. Many think that because of this, China is incompatible with the WTO and should not be a part of it. Staiger argues that instead, China should be told that they need to honor the market access reciprocity of the WTO.

Summary of Episode 181:

The trade war between the US and China started in 2018 and has yet to come to an end. There was a truce three years ago, but most of the tariffs are still in place. Trump started an investigation into China's trade practices in 2017 with the most notable aspect being the trade deficit. He gave subsidies to US farmers, but not to other sectors that faced negative consequences of the trade war, like the manufacturing sector. This is likely because farming communities are likely to vote Republican, so

Trump wanted to strengthen their political support of him. The US and Chinese presidents seemed to come to an agreement, and then the trade war was back on in May 2019.

Trump claimed that China had paid for $60 billion worth of tariffs, but research would show that the US consumers were actually the ones that paid for the tariffs. Trump and the Chinese president met and came to an agreement in 2020. When Biden came in to office, he essentially ignored trade with China and focused on more domestic issues, the pandemic, and trade with European allies as well as South Korea and Japan.

Trump made claims that over two years, China would pay for $200 billion of imports from the US. Brown states that his team added up the data and exactly none of the imports Trump promised they would buy. He explains that without the trade war, US exports would be much higher. Now, they are 23% lower than the benchmark for if they had grown at an average rate. The trade war caused Tesla to open a plant in China because it was not profitable to export from the US, and the US has not recovered their pre trade war auto-exports to China. Boeing has suffered as well because China switched to buying European Airbus planes. The US was able to recover a bit when Russia cut off energy supplies to Europe and America stepping to supply coal and oil.

Part II: Worked Problems

1. (Chapter 1 Q6) The relative size of international capital flows may not be greater today than they were 100 years ago, although they are certainly greater than they were 50 years ago. Qualitatively, however, capital flows are different today. Explain.

The quality of international capital flows is better today because we have developed technology that facilitates global trade and encourages globalization. First, more people are able to participate in international trade. For example, many average Americans have started buying skincare products from Korea. Anyone with $10-20 can buy face wash and moisturizer straight from another country with a few clicks. Additionally, the information available through the Internet provides consumers with more options that they may never have known about before. Also, technology has greatly increased efficiency in logistics. Sellers can receive orders from buyers instantaneously if via a website or app. This speeds up shipping times, making global trade more efficient, available, and practical in everyday life for millions of people. Countries are now very interconnected through technology, which greatly contributes to globalization in terms of economics and otherwise.

2. (Chapter 3 Q1) Use the information in the following table on labor productivities in France and Germany to answer questions a through e

Output per hour worked

	France	**Germany**
Cheese	2 kilograms	1 kilogram
Cars	0.25	0.50

1. Which country has an absolute advantage in cheese? In cars? **France has an absolute advantage in cheese production and Germany in car production.**

2. What is the relative price of cheese in France if it does not trade with Germany?

   2/0.25 = 8, so one car costs 8 kilograms of cheese

3. What is the relative price of cheese in Germany if it does not trade with France?

   1/0.50 = 2, so one car costs 2 kilograms of cheese

4. What is the opportunity cost of cheese in France? In Germany?

   France: 8 kilograms of cheese per car

   Germany: 2 kilograms of cheese per car

5. Which country has a comparative advantage in cheese? In cars? Explain.

   France has a comparative advantage in cheese because it costs only .25 cars to make 2 kilograms of cheese, while it would cost Germany 1 car to make 2 kilograms of cheese. Germany has the comparative advantage in cars because it would cost 0.5 kilograms of cheese to make one car, while it would cost France 8 kilograms of cheese to make one car.

6. What are the upper and lower bounds for the trade price of cheese?

   Upper bound: 8 kilograms of cheese per car

   Lower bound: 2 kilograms of cheese per car

3. (Chapter 4 Q1) According to the following table, which country is relatively more labor abundant? Explain your answer. Which country is relatively more capital abundant?

	US	Canada

Capital	40 machines	10 machines
Labor	200 workers	60 workers

Canada is more labor abundant because they have 6 workers per machine, while the US only has 5 workers per machine. The US is more capital abundant because they have 0.2 machines per worker, while Canada has 0.167 machines per worker.

4. (Chapter 4 Q2) Suppose the United States and Canada have the factor endowments in the preceding table. Suppose further the production requirement for a unit of steel are two machines and eight workers, and the requirements for a unit of bread is one machine and eight workers.

   a. Which good, bread or steel, is relatively capital intensive? Which good is relatively labor intensive? **Steel is relatively more capital intensive because it requires .25 machines for every worker while bread only requires .125 machines per worker. Bread is relatively more labor intensive because it requires 8 workers per machine while steel requires 4 workers per machine.**

   b. Which country would export bread? Why? **Canada would export bread because it is a relatively more labor intensive good than steel and Canada is relatively more labor abundant than the US.**

5. (Chapter 4 Q6) Describe the changes in production requirements, and location of production that take place over the three phases of the product cycle.

In the introduction phase, the production requirements are low because not all target consumers are aware of the product. The location of production is close to the market, so in the same country/region that the good is being sold. In the growth phase, the production volume increases because the firm is seeing increased demand for the product. Here, the firm will start to look at producing in places with lower production costs and making sure their supply chain is efficient. In the maturity phase, production volume will stabilize/plateau and the firm is likely to look for the lowest production costs offered by other countries. In the decline stage, production will decrease, as the demand for the product has decreased. The firm will continue to produce from the location with the lowest costs.

(Chapter 5 Q4) What are three key incentives for firms in a particular industry to cluster together in a geographic region?

1. A geographic industrial region attracts highly skilled workers in that industry because they want more job opportunities. An example is how Silicon Valley is home to the biggest tech companies and also some of the best tech experts and innovators.
2. Clustering reduces costs in the supply chain. For example, if the best suppliers of apples are located in one region, the producers of apple juice, ciders, and apple

sauce in that region would benefit from lower shipping costs of apples because they are nearby.

3. There could also be knowledge spillovers within the industry. If many people in the same industry are located in the same place, there would be lots of interactions between employees/firms in this industry, whether formal or informal.

6. (Chapter 5 Q6) When the United States signed a free-trade agreement with Canada (1989) no one thought twice about it. When the agreement with Mexico was signed (1994), there was significant opposition. Use the concepts of inter industry trade and intra-industry trade to explain the differences in opposition to the two trade agreements.

When the US and Canada signed a free trade agreement, the two countries intended to trade intra-industry, primarily with cars and car parts. The nations were similar in economic terms of capability and stability. Essentially, America and Canada were similar countries trading similar items, so no one thought it would cause any problems. Mexico, on the other hand, wanted to engage in inter industry trade with the US. They also had a much different economic situation than the US; the labor costs were much cheaper, so opponents of NAFTA feared that US jobs would shift to Mexico because the wage levels would cost firms less money.

7. (Chapter 6 Q2) Suppose the world price for a good is 40 and the domestic demand and supply curves are given by the following equations:

Demand: $P = 80 - 2Q$

Supply: $P = 5 + 3Q$

a. How much is consumed? **40 = 80 - 2Q, 2Q = 40, Q = 20 units**

b. How much is produced at home? **40 = 5 + 3Q, 3Q = 35, Q = 11.67 units**

c. What are the values of consumer and producer surplus?

Consumer surplus: (0.5)(80 - 40)(20) = 400

Producer surplus: (0.5)(40 - 5)(11.67) = 204.225

d. If a tariff of 10 percent is imposed, by how much do consumption and domestic production change?

P = 40 + (.10*40)

P = 44

44 = 80 - 2Q

Q = 18 consumed

44 = 5 + 3Q

Q = 13 produced

e. What is the change in consumer and producer surplus?

Change in consumer surplus = (0.5 * (44 - 40) * 18) - (0.5 * (80 - 40) * 20)

Change in consumer surplus = -364

Change in producer surplus = (0.5 * (44 - 5) * 13) - (0.5 * (40 - 5) * 11.67)

Change in producer surplus = 49.28

f. How much revenue is generated by the tariff?

Tariff revenue = 0.10(18 - 13) = 0.5

g. What is the net national cost of the tariff?

Net national cost of tariff: -364 + 49.28 + 0.5 = -314.22

8. (Chapter 9 Q2). Look at each of the following from the point of view of the balance of payments for the United States. Determine the subcategory of the current account or financial account that each transaction would be classified in, and state whether it would enter as a credit or debit.

a. The U.S. government sells gold for dollars. **Credit, financial**

b. A migrant worker in California sends $500 home to his village in Mexico. **Debit, current**

c. An American mutual fund manager uses deposits of his fund investors to buy Brazilian telecommunication stock. **Debit, financial**

d. A Japanese firm in Tennessee buys car parts from a subsidiary in Malaysia. **Debit, current**

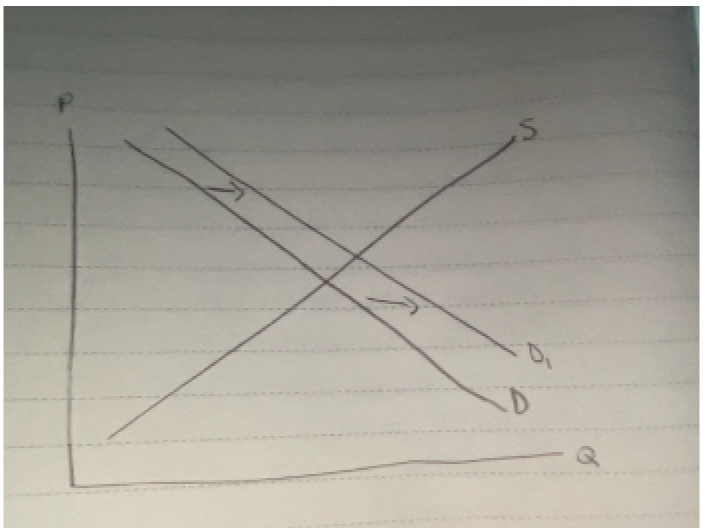
e. An American church donates five tons of rice to the Sudan to help with famine relief. **Debit, current**

f. An American retired couple flies from Seattle to Tokyo on Japan Airlines. **Debit and current**

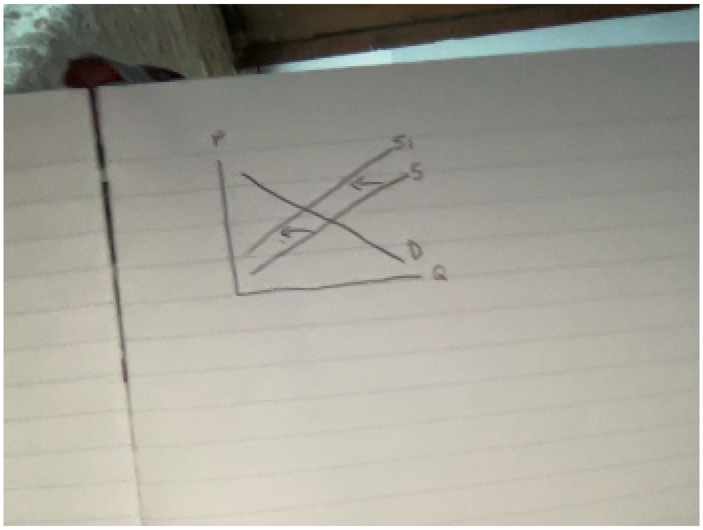
g. The Mexican government sells pesos to the United States Treasury and buys dollars. **Debit, financial**

9. (Chapter 10 Q1) Draw a graph of the supply and demand for the Canadian dollar by the U.S. market. Diagram the effect of each of the following on the exchange rate: state in words whether the effect is long, medium, or short run and explain your reasoning.

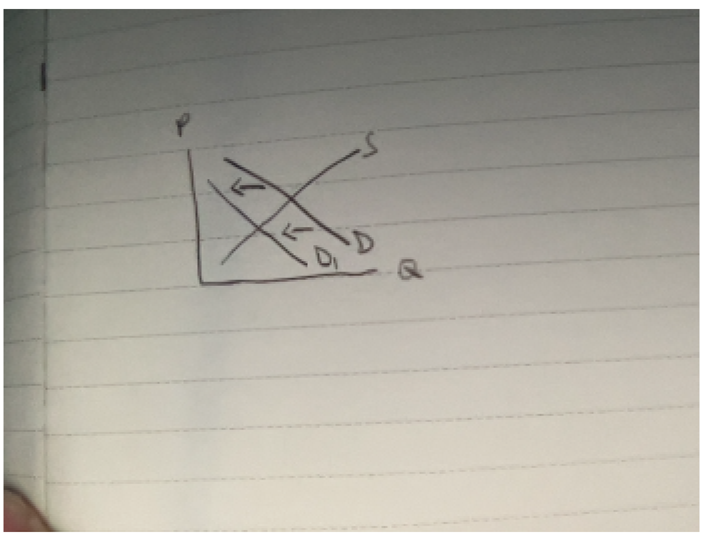
a. More rapid (economic) growth in Canada than in the United States. **This would increase demand for the Canadian dollar. This is medium or short run because it is due to a cyclical upswing or downswing in Canada's economy.**



b. A rise in U.S. interest rates. **This would decrease the supply of canadian dollars because demand for US dollars would increase, causing more canadian dollars to be converted into USD to take advantage of lower interest rates. It would affect the short to medium term because changes in interest rates have immediate rather than long term effects.**

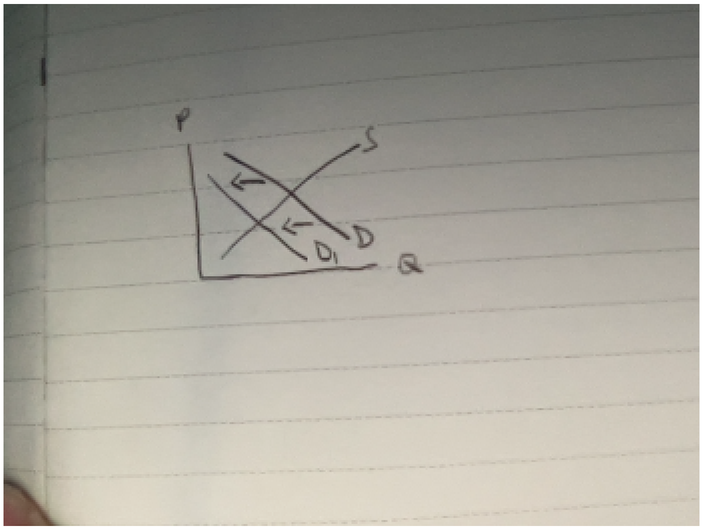


c. Goods are more expensive in Canada than in the U.S.. **This will decrease the demand for canadian products, and therefore decrease the demand of the canadian dollar. This will affect the medium term as changes in the overall price level of a country's goods can take a while to return to normal.**



d. A recession in the U.S. **will decrease demand in the US for imports, including those from Canada, which will decrease demand for the canadian**

dollar. This will affect the medium to long term, depending on the duration of the recession in the US.



e. Expectations of a future dollar appreciation. **If people think the canadian dollar will gain more value in the future, they will demand more now, so that their money will appreciate. This will affect the short to medium term because expectations and predictions can change as new information is revealed.**