

NEW YORK UNIVERSITY
Stern School of Business - Undergraduate Division

C45.0001
Economics of International Business

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Fall 1999

Overview: Understanding the global economy is key to success in a broad range of business and financial decisions. This course is a fast-paced survey of international economics. It is intended to provide the participants with frameworks that they can use to discuss and analyze the global economic environment within which businesses operate. The topics covered include the theory of international trade, government policies toward imports and exports, the balance of payments, foreign exchange markets, and international financial investment. Emphasis is placed on the determinants and effects of international economic linkages, including the role of government policies.

Objectives: The minimum objective for this course is that students acquire knowledge of the fundamental principles and issues in international economics. As such, students should be able to define basic terminology, to state important relationships and to identify the key issues in international economics. Moreover, students should be able to demonstrate their comprehension by describing important economic processes (e.g. the gains from international trade in commodities and the pattern of international capital flows) and by comparing alternative economic systems (e.g. the economic effects of tariffs versus quotas and international adjustment under pegged versus flexible exchange rates). Finally, since much of the emphasis in this course is on analytical models and since the theories have numerous practical implications, students should be able to formulate economic interpretations and explanations of current international events (e.g. proposals for other nations to voluntarily limit their exports to the United States, or proposals to abandon a fully flexible exchange rate system in favor of a target zone or a currency board system).

Prerequisites: All students must have completed the stated prerequisites, A31.0001 (Principles of Microeconomics) and A31.0002 (Principles of Macroeconomics) *prior to* registering for this course. No exceptions will be granted to this requirement.

Required Text and Readings: The primary textbook for the course is:

Peter H. Lindert and Thomas A. Pugel, International Economics, Tenth Edition, Irwin, 1996. (Referred to as LP)

In addition, a Study Guide by Kerry Odell is available. It is not required, but some students find it useful.

There are dozens (or probably hundreds) of textbooks on International Economics. Students may find it helpful to consult another text to read an alternative description or analysis. Two textbooks that I have used in the past are:

International Economics by Militades Chacholiades (New York: McGraw-Hill): 1990. [Bobst call number HF1411.C412 (1990)]

which is particularly good on international trade theory and trade policy topics, and

International Economics: Theory and Policy, Fourth Edition, by Paul Krugman and Maurice Obstfeld (New York: Harper Collins): 1997. [Bobst call number HF1359.K78 (1997)]

which is particularly good on international financial theory and policy topics. Both of these books will be placed on reserve.

In addition, a few articles on important topics are listed throughout the reading list when these articles are easily available through the internet.

Other Course Materials: Several problem sets will be distributed during the course. The problem sets need not be handed in; rather, suggested answers will be distributed. You may wish to form informal study groups with other students to discuss the problem sets or meet with the class teaching assistant to clarify any questions about the problem sets.

In addition, it is highly advisable during the semester to keep up with current developments in the field of international economic relations, both for class purposes and for your own benefit. This can best be done by reading the relevant current articles in: (a) the business section of the *New York Times*, the *Wall Street Journal* or the *Financial Times*; (b) the *Economist* (weekly); and (c) other weekly news magazines. Students are strongly encouraged to bring up current problems for discussion in class, as time permits. Copies of recent newspaper articles and items relevant to the course topics will be distributed from time to time in class or posted on the course web page.

The course outline and the course web page (at www.stern.nyu.edu/~rlevich/f1999/home.htm) contain links to various international economic policy making or research bodies. You may want to visit some of these sites to become more familiar with current international policy issues and how the analytical tools in this course are applied in practice.

Course Requirements and Evaluation: The course grade will be based on the following items:

Take home early mid-term examination	15%
In-class mid-term examination	25%
In-class final examination	35%
First written country assignment	10%
Second written country assignment	15%

The take-home early mid-term examination covers Topics 1-4 of PART ONE. It will be distributed on September 30 and due on October 12.

The in-class midterm examination covers all of PART ONE, with concentration on Topics 5-7. It will occur on November 2.

The in-class final examination covers PART TWO of the course.

The examinations cover material contained in the class sessions, readings, problem sets, and other class handouts.

Each student can bring one sheet of paper (8½ x 11) with notes on both sides to use during each in-class examination. Otherwise, the in-class examinations are closed book.

Specific instructions for the written country assignments are at the end of this course outline and also posted on the course web page. The written assignments are group assignments. The first written assignment covers material in the first portion of PART ONE of the course. It will be due on October 21. The second written assignment covers material in PART TWO of the course. It will be due on December 2.

Class Teaching Assistant: Mr. Jiawei Hu is the class teaching assistant. His office hours are Monday (2:00-3:30 pm) and Thursday (2:00-3:30 pm) and by appointment in KMEC Room 7-174. Mr. Hu will also conduct several optional review sessions before each in-class exam. Telephone 212-998-0411; e-mail jhu0@stern.nyu.edu [the 0 is a zero]

HOW TO REACH ME

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E-mail: rlevich@stern.nyu.edu

My Secretary: Ms. Robyn Vanterpool, Phone: 212-998-0702;
E-mail: rvanterp@stern.nyu.edu

Course Web Page: www.stern.nyu.edu/~rlevich/f1999/home.htm Watch this page for course announcements, due dates of assignments, and other information.

Course Outline and Reading List

Part One: International Trade

Classes 1 and 2, September 7 and 9

1. Introduction and Review of Analytic Concepts

Scope and content of international economics

International economics as a distinct discipline

Review of microeconomic analytical concepts: Demand, supply, production, consumption, utility, equilibrium, and so forth.

Partial equilibrium analysis and international trade: Effects on prices and quantities, consumer and producer surplus, net national gain.

Readings: LP, Chapters 1 and 2.

Classes 3-5. September 14, 16, and 21

2. The Theory of International Trade

Classical theory (Ricardo): Constant opportunity costs, absolute and comparative advantage, terms of trade, gains from trade.

Factor proportions theory (Heckscher-Ohlin): Increasing opportunity costs, factor endowments, factor price equalization, effects on income distribution, Stolper-Samuelson theorem.

General equilibrium analysis: Offer curves, determination of world price ratio

Empirical evidence: Leontief paradox

Readings: LP, Chapters 3 and 4, Appendix C.

Class 6. September 23

3. Economic Growth and Trade

Factor growth, Rybczynski theorem, technological progress, immiserizing growth

Readings: LP, Chapter 5.

Class 7. September 28

4. Extensions of Classical Trade Theory

Product cycle, increasing returns to scale, monopolistic competition, intra-industry trade

Readings: LP, Chapter 6.

TAKE-HOME EARLY MID-TERM EXAMINATION DISTRIBUTED

Classes 8-10. September 30, October 5 and 7

5. The Theory of Commercial Policy

Partial equilibrium analysis of trade barriers: Effects of tariffs, “deadweight” losses, tariffs versus quotas versus subsidies, voluntary export restraints (VERs) and other non-tariff barriers, effective rate of protection

General equilibrium analysis of trade barriers: Terms of trade effect, optimal tariff, theory of the “second best”

Arguments for and against tariff protection: Specificity rule, infant industry argument, dying industry argument, government revenue, national defense, adjustment assistance

Measuring the cost of protection: Share of GDP, income distribution, dynamic effects

Political economy of protection: General Agreement on Tariffs and Trade (GATT) and World Trade Organization (WTO), economics and politics of trade liberalization

Readings: LP, Chapters 7, 8, and 9, and pages 276-281, and Appendix D.

Robert Baldwin, "The Political Economy of Trade Policy," Journal of Economic Perspectives, Fall 1989. (www.xxxx.zzzz)

Classes 11 and 12. October 12 and 14.

6. “Unfair“ Trade and Export Policies

Dumping, antidumping duties, export subsidies, countervailing duties, strategic trade policy, market access, Section 301

Readings: LP, Chapter 10

Class13. October 19.

7. Discriminatory Trade Policies

Types of integration schemes: Free trade area, customs union, common market, and economic union; static and dynamic effects of integration

Trade creation and trade divergence effects

Regional trade blocs (NAFTA, LAFTA, ASEAN, MERCOSUR) versus global trade policies

Readings: LP, Chapter 11 (pages 201-214 only)

Part Two: International Finance

Classes 14 and 15. October 21 and 26.

1. The Balance of Payments: Concepts and Accounting

International trade in securities: Inter-temporal trade, gains from trade, life cycle of consumption, savings and wealth.

Accounting conventions

Current account: goods, services and unrequited (unilateral) transfers

Capital account: non-official short-term and long-term capital flows

Statistical discrepancy: Net errors and omissions

Official settlements balance, official reserve account

Alternative definitions of "balance": Balance in the short-run and the long-run, sustainable and unsustainable balances, temporary and permanent imbalance (disequilibrium)

International investment position: Debtor and creditor nations

Readings: LP, Chapter 15.

David Howard, "Implications of the U.S. Current Account Deficit," Journal of Economic Perspectives, Fall 1989. (www.xxxx.zzzz)

NOTE: CLASS 17, NOVEMBER 2 – IN-CLASS MID-TERM EXAMINATION

Classes 16 and 18. October 26 and November 4

2. The Foreign Exchange Market and International Financial Investment

Organization and institutional features

Terminology: Spot and forward contracts, European and American terms, appreciation/depreciation, premium/discount, brokers, dealers, hedging, speculation, arbitrage

Recent exchange rate behavior: Nominal rates, effective rates, real effective rates

Introduction to spot and forward rate determination: Private supply and demand, central bank intervention

Covered international financial investment: Covered interest parity, covered interest arbitrage and the "Lake" diagram

Uncovered international financial investment

Readings: LP, Chapters 16 and 17.

Classes 19 and 20. November 9 and 11.

3. Determination of Exchange Rates in the Long-Run and the Short-Run

Long-run determinants of exchange rates: Purchasing power parity and the monetary approach

Short-run determinants of exchange rates: The asset approach, exchange rate overshooting, bandwagon and momentum effects

Empirical evidence on exchange rates in the long and short-run

Forecasting exchange rates in the long and short-run

Readings: LP, Chapters 18 and 19.

Classes 21 and 22. November 16 and 18.

4. Macroeconomic Policies Under Fixed Exchange Rates

Internal and external balance

Linkages among the goods market, money market and foreign exchange market

The impact of monetary policies under fixed exchange rates: Hume's price-specie-flow mechanism

The impact of fiscal policies under fixed exchange rates

Can a change in the exchange rate bring about adjustment and improvement?
Devaluation and relative prices, J-curve, role of elasticities, Marshall-Lerner condition

Readings: LP, Chapters 21 and 22, and Appendix G

Classes 23 and 24. November 23 and 30. (No class on November 25, Thanksgiving)

5. Macroeconomic Policies Under Floating Exchange Rates

The impact of monetary policies under floating exchange rates

The impact of fiscal policies under floating exchange rates

International macroeconomic policy coordination

Policy instruments and targets, policy conflicts and policy efficiency, the assignment problem, sterilization, the role of capital mobility

Readings: LP, Chapter 23

Classes 25 and 26. December 2 and 7.

6. Policy Choices for the International Monetary System

Historical experience with alternative systems: Gold standard, the inter-war years, the Bretton Woods Agreement, European Monetary System

Policy options: Discretion versus rules, automatic adjustment mechanisms, exchange and capital controls

Choosing between fixed versus flexible exchange rates

Intermediate choices: Managed floating, target zones

Defending a fixed rate: Central bank intervention, stabilizing and destabilizing speculation, exchange controls

The International Monetary Fund: Surveillance, conditionality, transparency

Optimum currency areas, European Economic and Monetary Union (EMU) and the Euro

Currency boards, “dollarization“

Readings: LP, Chapters 20 and 24.

Class 27. December 9.

Review session and open discussion

Final Examination – Date to be announced