Final Econ 2260 Driskill

Essays (short), true-false

1. 10 points. Explain what economics mean by "gains from trade."

There exists a hypothetical redistribution of resources under free trade such that, if this redistribution took place, and it was costless, then at least someone would be better off and no one would be worse off than was the case under autarky. It could be that everybody would be better off. A thought experiment: it doesn't say that compensation takes place. In reality, paying compensation would be problematic and would use up resources.

2. 20 points. The author of "Travels" started her investigation because of concerns by her students about working conditions in the textile and apparel industries around the world. Based on your readings in "Travels," respond to the notion that rich-country consumers should boycott clothing made in less-developed countries because of working conditions in those locations.

A: "sisters in time:" beats the farm. What else?

3. 20 points (5 points each). On page 156, the author of "Travels" poses the following question:

"How did the United States–as the self-anointed free trade champion of the universe–end up with such a dauntingly complex and downright silly mass of barriers to the import of T-shirts? Why, in an era of progressive trade liberalization and increasing deference to the market mechanism, has the role of politics remained so pervasive in this industry?" According to Rivoli in TT, this is

a. _____in part because the RTAA gave bargaining power to importers.

Falso. It created it for exporters.

b. _____in part because of geographic concentration among textile and apparel producers.

Si.

c. _____in part because t-shirt retailers are a diffuse group.

Si.

d. _____in part because other manufacturing industries worried that they could be next sector suffering from low-cost import competition.

Si.

4. 20 points (5 points each). The idea of "gains from trade" might *at best* be viewed as concerning the **long-run** prosperity of a country because

a. _____in the long run, a society that embraces changes in economic circumsances that satisfy the compensation principle might likely have most people in the society at some future time better off than they would have been if the status quo had been enforced.

True

b. _____in the short run there are almost surely some losers.

True:

c. _____whether in the long run or short run, more people gain from trade than lose.

False.

d. _____whether in the long run or short run, voluntary trade must make a country better off than aurarky, other wise it wouldn't do it.

False

Note: In the short run, winners and losers, hard to compensate. Over time, an economy htat embraces PPI's might make the 'average" person better off, as she wins sometimes, loses other times, but since all are PPI's, will be better off over time.

5. 20 points. Smoot-Hawley was passed in 1930 and led to How did the Reciprocal Trade Agreements Act help the United States lower tariff barriers?

6. True-false. 10 points total. Two (2) points for each correct answer. If you want, you can argue your case with a few short sentences of explanation for your choice.

a. _____In contrast to U.S. anti-dumping laws, the purpose of domestic anti-trust laws has been interpreted by the U.S. supreme court to be "the protection of competition, not competitors."

b. _____The Reciprocal Trade Agreements Act brought exporters into the political process as a "concentrated" interest group on the side of tariff reductions.

c. _____The World Bank, the IMF, and (eventually) the WTO, are known as the Bretton Woods institutions in honor of the English statesman Sir Bretton Woods who is usually credited as the architect of the agreements that led to the establishment of these organizations.

d. _____Economic theory tells us that in the long run, the bilateral current account balance between the U.S. and China should be zero.

e. _____Warren Buffett is a Republican because he believes their stance on free trade promotes the well-being of the country better than the protectionist policies advocated by Democrats.

7. 10 points. As countries contemplated forming the Eurpean Common Market (forerunner to the EU), observers worried that resulting import competition in industries like the auto industry would unleash protectionary pressures that would make the ECM short-lived. Why were these observers wrong?

8. 20 points. One argument that appears to be used by the Trump Administration to justify its trade war with China is that China steals our intellectual property rights. Address this argument (it may help to consider the following quote form TT):

"Using his significant mathematical aptitude, Lowell memorized the critical details of Edmund Cartright's power loom and returned home to Massachusetts. While Lowell's act was exceptional in securing for America the crown-jewel technology of the power loom, complementary technology also leaked into the United States during this period, most often in the minds of skilled artisans from Britain who had managed to evade emigration restrictions. By 1812, virtually all of the important technology related to cotton textile production had been transferred to New England."

Rivoli, Pietra. The Travels of a T-Shirt in the Global Economy: An Economist Examines the Markets, Power, and Politics of World Trade. New Preface and Epilogue with Updates on Economic Issues and Main Characters (p. 97). Wiley. Kindle Edition.

Macro

Money and nominal prices. 20 points.

1. Consider the monetary side of two real economies. Money demand is given as (we normalize real income to one (1)):

$$L^d = \frac{1}{2}P_I;\ L^{*d} = \frac{1}{2}P^*_{I^*},$$

where the price indices are given as a weighted average of the three nominal prices:

$$P_I = \frac{1}{3}P_X + \frac{1}{3}P_M + \frac{1}{3}P_N;$$
$$P^*_{I^*} = \frac{1}{3}P^*_X + \frac{1}{3}P^*_M + \frac{1}{3}P_N;$$

Money supplies are exogenous and given as $\overline{L}$, $\overline{L}^*$, respectively:

$$\overline{L} = \overline{L}^* = 1.$$

In equilibrium, money demand equals money supply.

Relative prices are given as

$$\frac{P_X}{P_N} = \frac{P_X^*}{P_N^*} = \frac{P_M}{P_N} = \frac{P_M^*}{P_N^*} = 1.$$

Solve for P_N and P_N^*.

FX: 30 points.

In 1992, Britain was attempting to maintain a fixed exchange rate with respect to the German Deutschmark. It was also facing recessionary pressures, and did not want to raise its own interest rates. Germany raised its interest rate to finance reunification. Describe the problems this posed for Great Britain. Expository devices such as graphs would probably help your story.

BOP (we haven't done this yet)

Consider a hypothetical nation (say, the nation of Driskill) which has three citizens: Alex, Bobby, and Charley. This nation exists for two periods, period 1 and period 2. Alex exports $X^A_{Z,1}$ dollars worth of goods and services to citizens of the nation of Zeppos in period 1, and $X^A_{Z,2}$ dollars worth of goods and sevices to citizens of Zeppos in period 2. Alex also loans amount $LT^A_{B,1}$to bobby in period 1, and receives repayment amount $(1+r)LT^A_B$ from Bobby in period 2. Bobby imports $M^B_{Z,1}$ and $M^B_{Z,2}$ dollars worth of goods from the nation of Zeppos in periods 1 and 2, respectively. Bobby exports $X^B_{C,2}$ to citizens of country AF in period 2. Bobby also borrows amount $BF^B_{A,1}$ in period 1 and repays $(1+r)BF^B_{A,1}$ to Alex in period 2. Charley imports $M^C_{UT,1}$ dollars worth of goods and services from citizens of country UT in period 1 and exports $X^C_{MM,1}$ to citizens of country MM in period 1 and $X^C_{MM,2}$ in period 2. Charley also imports $M^C_{AF,1}$ and $M^C_{AF,2}$ from citizens of country AF in periods 1 and 2, respectively. Alex borrows amount $BF^A_{MC,1}$ from residents of country MC and repays $BF^A_{MC,1}(1+r)$ to these residents in period two. These are all the transactions that take place between citizens of our hypothetical nation and residents of other countries.

1. What is the aggregate budget constraint for the citizens of country 1 for period one and period two?

Answer: First let's go individual by individual. In period one:

$$\overbrace{X^A_{Z,1} + BF^A_{MC,1}}^{receipts} = \overbrace{LT^A_{B,1}}^{\exp enditures}\ ;\ BF^B_{A,1} = M^B_{Z,1};\ X^C_{MM,1} = M^C_{UT,1} + M^C_{AF,1}.$$

Aggregate (add up over all three):

$$X^A_{Z,1} + X^C_{MM,1} + BF^A_{MC,1} = M^B_{Z,1} + M^C_{UT,1} + M^C_{AF,1}$$

In period 2:

$$X^A_{Z,2} + (1+r)LT^A_{B,1} = (1+r)BF^A_{MC,1};$$
$$X^B_{AF,2} = M^B_{Z,2} + (1+r)BF^B_{A,1};$$
$$X^C_{MM,2} = M^C_{AF,2}$$

Aggregate:

$$X^A_{Z,2} + X^B_{AF,2} + X^C_{MM,2} = M^B_{Z,2} + M^C_{AF,2} + BF^A_{MC,1}(1+r)$$

2. Show that the present value of exports equals the present value of imports.

Answer: Solve each period budget constraint for $BF^A_{MC,1}$:

$$BF^A_{MC,1} = \overbrace{M^B_{Z,1} + M^C_{UT,1} + M^C_{AF,1}}^{\text{value of imports in pd 1}} - \overbrace{[X^A_{Z,1} + X^C_{MM,1}]}^{\text{value of exports in pd 1}}$$

$$BF^A_{MC,1} = \frac{1}{1+r}[X^A_{Z,2} + X^B_{AF,2} + X^C_{MM,2} - (M^B_{Z,2} + M^C_{AF,2})]$$

Equate and rearrange to get:

$$M^B_{Z,1} + M^C_{UT,1} + M^C_{AF,1} + \frac{1}{1+r}(M^B_{Z,2} + M^C_{AF,2})$$
$$= X^A_{Z,1} + X^C_{MM,1} + \frac{1}{1+r}(X^A_{Z,2} + X^B_{AF,2} + X^C_{MM,2})$$

3. The bilateral trade balance surplus for any period is defined as the value of exports from one country to another minus the value of imports between the two countries. Must the country of Driskill have a zero bilateral trade balance surplus with the country of Zeppos?

Answer: No. All that is required is that the present value of total exports equal the present value of total imports.

4. Why don’t we need to record loans between members of country 1 in order to compute the aggregate budget constraints?

Answer: They cancel out: a loan from citizen #1 to citizen #2 is an asset for #1 and a liability for #2.

More

1. 20 points. "Between 1880 and 1930, cotton textile production gradually withered in New England and took root in the southern Piedmont region. 27 The main draw to the South was lower wages: Wages in the North Carolina textile industry during this period were generally 30 to 50 percent lower than those paid to textile operatives in Massachusetts. ... In a precursor to today’s call for global labor standards, the New England industrialists argued that their industry’s only hope lay in convincing lawmakers to legislate working conditions and hours in Southern factories so that the lack of worker protections in the South could not be used to its competitive advantage." (Rivoli, Pietra. The Travels of a T-Shirt in the Global Economy: An Economist

Examines the Markets, Power, and Politics of World Trade. New Preface and Epilogue with Updates on Economic Issues and Main Characters (p. 100). Wiley. Kindle Edition.)

How does this passage inform your thinking on the "creative destruction" that has moved industries from one part of the world to another?

2. 20 points. Trace the history of the "chicken wars," and comment on the unintended consequences of the war.

3. 20 points. How have trade restrictions lead to "Directly unproductive activities"?