International Economics 17th edition Pugel Solutions Manual

SKU: 9781260004731-SOLUTIONS

Chapter 1

International Economics Is Different

Overview

The introduction to the subject of international economics has three major purposes:
1. Show that international economics addresses important and interesting current events and issues.
2. Show why international economics is special.
3. Provide a broad overview of the book.

We begin with four controversies that show the importance of current issues addressed by international economics.

The first controversy examines the views of U.S. President Donald Trump and his trade policy actions during his first two years in office, which led to the largest trade war since the Great Depression. Soon after his inauguration in 2017, Trump withdrew the United States from the Trans-Pacific Partnership, and later that year he commenced the process of renegotiating the North American Trade Agreement with Canada and Mexico. In early 2018 he imposed temporary safeguard tariffs on imports of washing machines and solar panels. Then, following investigations which found that imports of steel and aluminum were threats to national security, in March 2018 Trump imposed tariffs, with temporary exemptions for a number of countries. His administration induced South Korea and Argentina to accept "voluntary" steel export restraints and imposed quotas (instead of tariffs) on steel imports from Brazil. In June Trump ended the temporary exemptions and imposed tariffs on imports of steel and aluminum from Canada, Mexico, and European Union (EU) countries. The first front of the trade engaged as China, Mexico, the EU, and Canada imposed retaliatory tariffs on imports from the United States.

The second front of the trade war began as a U.S. Section 301 case. The Trump administration concluded that the Chinese government was using and continued to use unfair policies and practices to gain access to the technologies and other intellectual property of U.S. firms. In March 2018 Trump decided to bring a case to the World Trade Organization (WTO) and threatened tariffs on U.S. imports from China unless the Chinese government changed its policies. In July Trump imposed tariffs, and the Chinese government immediately retaliated with tariffs on imports from the United States.

Trump's trade policies and the trade war involve topics that are central to Chapters 2-16 of the book, including:
- National gains from international trade (both imports and exports, not at the expense of other countries).
- National and global effects of tariffs, quotas, and voluntary export restraints.
- The potential for a large country to shift international trade to gain additional national benefits.

© 2016 by McGraw-Hill Education. This is proprietary material solely for authorized instructor use. Not authorized for sale or distribution in any manner. This document may not be copied, scanned, duplicated, forwarded, distributed, or posted on a website, in whole or part.

International Economics 17th edition Pugel Solutions Manual

- The risk of retaliation by other countries, and the likelihood that all countries in a resulting trade war lose.
- The role of the WTO and the use of U.S. Section 301.
- The shortcomings of the national defense argument for protection.
- Dumping, antidumping duties, safeguard actions, export subsidies, and countervailing duties.
- The economics of free trade areas.
- Foreign direct investment and the global activities of multinational enterprises.
- The national trade balance as driven by the difference between national saving and domestic real investment.

As of late 2018 the trade war and effects of Trump's trade policy actions were still evolving.

The second controversy arises from international migration, especially the increasingly vehement complaints about immigrants in many of the major receiving countries. In these countries a rather large (10 percent or more) and rising percentage of the population is foreign-born, including many who are unauthorized. Opponents accuse immigrants of causing general economic harm, imposing fiscal costs as immigrants use government services, and increasing crime. International economics is often about emotional issues like immigration, yet we do our best to use economic analysis to think objectively about actual economic effects. In a preview of the analysis of Chapter 15, we highlight two key conclusions about the effects of immigration on the receiving country. First, as with many issues in international economics, there are both winners and losers in the receiving country. Second, we can determine the net effect on the receiving country. As we often conclude when we examine freer international exchange, the net national effect of immigration is positive according to the basic economic model, in this case even if we ignore the gains to the immigrants themselves.

The third controversy is about Britain's relationship with the rest of the European Union. A slim majority of U.K. voters in 2016 voted to leave the EU. While proponents of "remain" stressed the economic benefits of being part of the EU, proponents of "leave" stressed the need to reassert national sovereignty in such areas as control of immigration. After the controversial vote, the process of leaving (Brexit) brought new controversies, because the vote itself said nothing about the relationship that Britain would have with the EU after Britain separated. One surprisingly difficult issue quickly arose. Both the EU and Britain agreed that there should be no border checks along the land border between Ireland and Northern Ireland. But, as of late 2018 there was no agreement on how this could be achieved. More broadly, what are the government policies that will be applied to international trade between Britain and the EU? What tariffs and customs procedures? What nontariff barriers like product regulations and standards? What rules (which can raise barriers) will apply to trade in services (for British interests, especially financial services)? And, beyond trade, what policies will govern migration between Britain and the EU? A "hard Brexit" reasserts British sovereignty but would be very disruptive to businesses and markets. A "soft Brexit" is less disruptive but would mean that Britain would remain subject to many EU laws and regulations. Chapter 12 presents the economics of preferential trade agreements and the evolution of the EU from a customs union toward a single market and increasing economic union.

© 2016 by McGraw-Hill Education. This is proprietary material solely for authorized instructor use. Not authorized for sale or distribution in any manner. This document may not be copied, scanned, duplicated, forwarded, distributed, or posted on a website, in whole or part.

International Economics 17th edition Pugel Solutions Manual

The fourth controversy is the exchange rate value of the Chinese yuan. From the mid-1990s to 2005, the Chinese government maintained a fixed exchange rate of the yuan to the U.S. dollar. As China's trade surplus increased and the Chinese government continually had to enter the foreign exchange market to buy dollars and sell yuan to keep the exchange rate steady, the United States and the EU increasingly complained about the fixed rate. In 2005 the Chinese government began to allow gradual increases in the exchange-rate value of the yuan. In mid-2008, in response to the worsening global financial and economic crisis, the Chinese government reverted to a fixed exchange rate. Then, as the Chinese economy resumed its rapid growth and China's government continued to amass international reserves through its intervention to defend the fixed exchange rate, foreign pressures reemerged. In mid-2010 China's government again began to allow gradual appreciation of the yuan. By early 2014 most observers thought that the yuan was no longer undervalued.

In the controversy over China's exchange rate policy, we can see many of the issues that we will examine in Chapters 16-25 of the book, including the measurement and meaning of a country's balance of payments (including its trade balance), government policies toward the foreign exchange market and how a government defends a fixed exchange rate against market pressure for the exchange rate value to change, foreign financial investments and the role of currency speculators, political pressures that can place limits on how long a country with a fixed exchange rate and a trade surplus can maintain the fixed rate value, and how exchange rates affect not only a country's trade balance, but also its national macroeconomic performance (including production, employment, and inflation).

These four controversies show that international economics addresses important current issues. They also can be used to show why international economics is special—why national boundaries matter in economics. The first reason that international economics is special is that some resources do not move freely between countries. Land is essentially immobile. There are substantial impediments to the movement of labor internationally, as we see in the analysis of international migration, because of the personal and economic costs to people of moving from one country to another, and because of restrictive government policies. Financial capital moves more freely, but there still seems to be a home bias to many people's financial investments.

The second reason that international economics is special is that national government policies matter—in fact, they matter in two ways. One way is that national governments can adopt and change policies toward international transactions, as we see in President Trump's decisions to impose tariffs and other countries' decisions to retaliate with their own tariffs. The other way is that national governments adopt different economic policies. These national policies usually are designed to serve national interests, but they often have international effects. We see the tension between national interests and international effects in the discussion of China's exchange rate policy.

Tips for teaching

One good way to begin the first class session is with a look at current events, even before the mechanics and requirements of the course are presented. The instructor might use the day's

© 2016 by McGraw-Hill Education. This is proprietary material solely for authorized instructor use. Not authorized for sale or distribution in any manner. This document may not be copied, scanned, duplicated, forwarded, distributed, or posted on a website, in whole or part.

International Economics 17th edition Pugel Solutions Manual

newspaper (for instance, the *Financial Times* or *Wall Street Journal*) or the week's magazine (for instance, the *Economist* or *Business Week*) to highlight a few stories related to the content of the course. We have found that this is a good way to get the students' attention and interest. Another good beginning would be to provide a discussion that updates one or more of the four controversies in Chapter 1. For example, the instructor could look at the most recent information about U.S. trade policy (including the latest developments in or the aftermath of the trade war) or about the process and effects of Brexit.

You may want to consider beginning other class sessions of the course (not only the first class session) with a look at one or two stories in that day's newspaper. The stories should relate in some way to the material covered in the course, but they do not necessarily have to relate to the specific material covered in that day's session. We have found that this look at current events reinforces the relevance of international economic analysis. It also encourages students to read a good newspaper or magazine and to keep up with current events. In addition, we can model critical reading, if we both summarize the article's information and offer our own opinion or analysis (or ask the students for their opinions).

The instructor may also point out that there is a lot of information on international issues available on the Web. In additional to good newspapers and magazines that are available online, Figure A.1 in Appendix A provides a list of some important sites.

One issue in teaching is to get students to "take ownership" of the learning of the material. One good way to accomplish this is to get them to teach some of the material. In doing so they gain greater understanding as well as appreciation for the applicability of what sometimes sound like dry concepts and abstract issues. You may want to consider an assignment like the one that Pugel (and others at New York University) have been using successfully. It asks students working in groups to choose a topic based on current and recent events or developments and prepare and make a brief presentation to the rest of the class, during the second half of the course term. The accompanying pages under the heading "Sample Assignment" show a version of this assignment. It is good to get such an assignment set up early in the term, so that students have enough time to gather information and prepare the talk. One more thought—in evaluating each presentation, you may want to get the students in the audience involved by asking each to complete a brief evaluation form for each presentation.

© 2016 by McGraw-Hill Education. This is proprietary material solely for authorized instructor use. Not authorized for sale or distribution in any manner. This document may not be copied, scanned, duplicated, forwarded, distributed, or posted on a website, in whole or part.

International Economics 17th edition Pugel Solutions Manual

Sample assignment

NEW YORK UNIVERSITY
Stern School of Business

The Global Economy

Group Presentations

Each group will give a presentation to the class about one of the topics listed below. Your presentation is an opportunity to hone your research and presentation skills, to apply concepts from this course (and possibly from other courses), to attack a real issue, and to show off your creativity.

The formal presentation should last no longer than 15 minutes. In addition, after the presentation, you will have 5 minutes to take and answer questions from the class. I suggest you plan a talk that fills about 14 minutes to ensure that you finish within time. Going over the time limit for the presentation will result in a lower evaluation score for "style" and overall assessment.

For the oral part of the presentation, all group members must be involved in speaking. One aspect of the presentation is the ability to transition from one group member to the next as each in turn makes part of the presentation.

Evaluation will be based on three criteria:

- Informativeness: Information and data—how much did we learn from your presentation?
- Analysis and interpretation: Did you effectively use concepts and relationships from the course (and possibly from other courses) to analyze and/or interpret the information that you have? Were your conclusions sound? Did we gain novel insights into the topic?
- Style: Was your presentation logically structured, clear, and compelling? Were the slides effective? Did you keep within the time limit?

Above all, keep your classmates interested. If you use PowerPoint or similar slides, you should bring your presentation file to class on a USB memory stick.

Presentation Topics

Choose your topic from the list below. Topics will be allocated on a first-come, first-served basis. Each topic comes with a set of indicative questions. There is some scope to modify the questions, if you think it would lead to a more interesting presentation. Just ask me first.

After you know your topic, the group should search for information and start to plan the presentation. For many topics you can find much information on the Web. With Web research, it is up to you to verify that a source is credible and accurate.

© 2016 by McGraw-Hill Education. This is proprietary material solely for authorized instructor use. Not authorized for sale or distribution in any manner. This document may not be copied, scanned, duplicated, forwarded, distributed, or posted on a website, in whole or part.

International Economics 17th edition Pugel Solutions Manual

Here are the possible topics.

International Outsourcing/Offshoring of Services

Beginning in the 1990s, firms in the United States and other industrialized countries increasingly shifted service activities and jobs to developing countries, especially India. How large is this type of offshoring? How large could it be in the future? Why has it been controversial in the United States? Is it different from regular international trade? Should the U.S. government limit the ability of U.S. firms to send these jobs to other countries?

Do African Countries Trade Too Little with Each Other?

Countries that are closer to each other geographically tend to trade more with each other. Does this pattern hold as strongly across Africa as it does in other areas of the world? What do the data show? To the extent that African countries tend to trade less with each other than might otherwise be expected, how large is the "shortfall"? Why is there less international trade within Africa? Is the problem mostly a lack of free trade areas and similar bilateral and multilateral governmental agreements? Would African countries benefit from trading more with each other? What is the outlook for growing international trade within Africa during the next decade or so?

U.S. Imports of Tires from China

In mid-2015 the U.S. government imposed much higher tariff duties on U.S. imports of tires from China (by using U.S. antidumping and antisubsidy laws). This action comes several years after temporary high U.S. tariffs that were in effect during 2009-2012. Using economic analysis, how do tire markets adjust to the higher tariff duties? What is the economic analysis of winners and losers from this U.S policy action? What are the politics of imposition of the duties, both within the United States and internationally? Overall, do the tariff duties provide net benefits to the United States? If political pressure impels the U.S. government to do something, and with a view to maximizing net national economic benefit or minimizing net national economic cost, what is the best policy alternative that could be used instead of antidumping and antisubsidy tariff duties?

Trans-Pacific Partnership (TPP)

In October 2015 the United States and eleven other countries announced an agreement to form the Trans-Pacific Partnership, a new regional trade agreement, and the agreement was signed (but not ratified) in February 2016. What was the TPP in its original form? What were its key elements and features? What would have been the economics of the agreement for each of: the United States, Malaysia or Vietnam (an emerging country signatory), and a country like China (an emerging country that would not be a member)? In January 2017 President Trump withdrew the United States from the TPP. From the point of view of the U.S. national interest, was Trump correct to withdraw from the TPP?

© 2016 by McGraw-Hill Education. This is proprietary material solely for authorized instructor use. Not authorized for sale or distribution in any manner. This document may not be copied, scanned, duplicated, forwarded, distributed, or posted on a website, in whole or part.

International Economics 17th edition Pugel Solutions Manual

ASEAN

The member countries of ASEAN have committed to forming a true free trade area. What are the goals for this AFTA? How much progress has been made? Why has progress not been faster? Are there important issues that seem to thwart or limit the effort? What will happen over the next five years or so?

Cotton

U.S. policies toward cotton have become globally controversial. What are these policies? What effects do they have on the global cotton market? Why have the policies become controversial? How has the WTO been involved in efforts to alter U.S. cotton policies? How have U.S. policies toward cotton changed in recent years? What is the outlook for the next several years?

Locating a New Business Processing Center: India or Ghana?

A major firm in the business processing industry is looking to expand its capacity for providing call center and data entry services for its clients. It is considering locating a new facility in India, where it already has other facilities, or in Ghana, a country in which it does not currently operate. What are the strengths and weaknesses of Ghana, relative to India, as a location for this facility? What could the company request from Ghana's government if the company were to decide to locate the facility in Ghana? What would Ghana's government agree to provide to the company? Overall, would you recommend that the company locate its new facility in India or in Ghana? Why?

Ecuador

Ecuador dollarized in 2000. Why did the Ecuadorian government choose this policy? In what ways does it seem to have helped the Ecuadorian economy? In what ways has it hurt or caused problems or costs? Do you think that it was a good or bad idea for Ecuador to dollarize?

Sovereign Wealth Funds

Some national governments use sovereign wealth funds to invest in a wide range of international financial assets. How large are these funds? What are their funding sources? Are they like other international investors? Should countries receiving their investments be concerned? How should sovereign wealth funds be regulated?

Should Hong Kong Alter Its Fixed Exchange Rate Policy?

The Hong Kong government has maintained a fixed exchange rate between the Hong Kong dollar and the U.S. dollar for more than three decades. What are the advantages and disadvantages for Hong Kong of having this exchange rate policy? If the Hong Kong government is now considering changing its policy, what are two most likely alternative exchange rate policies that the Hong Kong government could adopt in place of the current fixed value to the U.S. dollar? What are the advantages and disadvantages of each of these? What is

© 2016 by McGraw-Hill Education. This is proprietary material solely for authorized instructor use. Not authorized for sale or distribution in any manner. This document may not be copied, scanned, duplicated, forwarded, distributed, or posted on a website, in whole or part.

International Economics 17th edition Pugel Solutions Manual

the case for Hong Kong to continue to fix at the current value to the U.S. dollar? What is the case for Hong Kong to switch to the next best alternative policy (one of the two you have examined)? What do think will actually happen during the next five years or so?

Internationalization of the RMB

Until a decade ago the Chinese yuan (or renminbi) was not much used internationally. In what ways, and to what extent, has this changed? Why? What are the benefits and costs to China from greater international use of the yuan? How could China promote greater international use? Should China do so? What do you think will happen in the next five to ten years? When will the yuan become the equal of the U.S. dollar in international uses?

Sweden To Join the Euro Area?

Sweden could be the next country to adopt the euro and join the euro area. Does Sweden qualify to join? What are the economic and political advantages to Sweden of joining? What are the economic and political disadvantages of joining? Should Sweden join the euro area in the next few years? Do you think that Sweden actually will join the euro area in the next few years?

Financial Flows to Developing Countries

As shown in Figure 21.2, net financial flows to developing countries in 2015-2016 fell to levels much lower than the inflows during 2010-2014. What are the possible causes of the 2015-2016 slowdown? Which of these possible causes actually explain the slowdown? To what extent should national governments in developing countries be worried about the slowdown? Why or why not?

Switzerland's Exchange Rate Policy

In August 2011 the Swiss economy faced challenges, and the Swiss government was reevaluating its policy toward the exchange rate value of the Swiss franc. What are the possible alternatives for its exchange rate policy that the Swiss government could have considered? What policy did the Swiss government actually implement? Why do you think it chose this new policy? How well did the new policy work during 2012-2014? In early 2015 the Swiss government again shifted its exchange rate policy. What letter grade would you give the Swiss government for its actual exchange rate policies during 2011-2015? Why?

What Country is Ripe for a Speculative Attack on Its Currency?

Identify a country that you think has a substantial probability of a speculative attack on the exchange rate value of its currency, sometime during the next several years. Why do think that a speculative attack may be imminent? If a speculative attack does not occur in the next several years, what do think will be the most likely explanation for why the attack did not occur? What do you think is the probability that a speculative attack on this currency will actually occur during the next several years?

© 2016 by McGraw-Hill Education. This is proprietary material solely for authorized instructor use. Not authorized for sale or distribution in any manner. This document may not be copied, scanned, duplicated, forwarded, distributed, or posted on a website, in whole or part.

International Economics 17th edition Pugel Solutions Manual