

Hong Kong University of Science and Technology
ECON 338
GLOBALIZATION: TRADE, INVESTMENT AND EXCHANGE RATE
Fall Semester, 2009-10 Academic Year
(OBE Pilot Course)

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General Information

Instructor: Dr. Yong Wang

Office: 2418 (Lifts 17&18)

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Phone: 2358-7625

OH: Wed 4:00-5:00 pm or by appointment

Lecture Time: Tue & Thu 9:00-10:20 am

Course Venue: 4006

Course Website: <http://ihome.ust.hk/~yongwang>

TA: Peter Tsui

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Phone: 2358-7597

OH: TBA (Room 2393)

Tutorial Time: Fri 5-5:50pm

Venue: Room 2502

Course Description

This course aims at helping students understand and analyze the real-world key phenomena and policies concerning economic globalization, an increasingly important feature of the modern world. The course has three parts. Part I discusses the causes, the patterns and the consequences of international trade without explicit policy interventions. Part II analyzes the welfare implications, the determinants, and the implementations of different trade policies. Part III focuses on financial globalization, which covers the analysis of the exchange rate, financial crisis, and macroeconomic policies. Fundamental models in international economics will be introduced with an emphasis on economic reasoning instead of mathematical formalities. Real world important globalization issues and policies will be discussed throughout the course, including the experiences of China and other Asian economies.

Learning Outcomes

After this course, students are expected to be able to (1) explain how the trade models work and their implications for income distribution and economic growth; (2) analyze relevant trade policies normatively and positively; (3) understand the key concepts and issues related with financial globalization such as exchange rate regime and financial crisis; (4) Identify and use the proper economic models to analyze relevant real-life globalization issues and policy debates.

Pre-requisites

ECON 110, 111 or 191 (or other equivalent knowledge of microeconomics)

Teaching Approach

This course is designed to help students cultivate the habit of thinking critically and independently but working constructively and cooperatively, as reflected in the grading policy. The basic teaching materials closely follow the main textbook and lecture notes. Two formal debates on some controversial policies will be held in class between two student teams, each of which is “politically” formed and intellectually supported by the students holding the same viewpoints. Students are highly encouraged to work collectively on the problem sets and prepare for the debates. Two exams will give students opportunities to demonstrate their abilities to analyze globalization while their abilities to think creatively and critically will be enhanced

through their efforts to meet the writing requirements. Active participation in class discussions is highly encouraged.

Requirement and Grading Policy

Mobile phones and any other disturbing electronic devices must be off during class time. Students are required to attend all the classes on time. Academic honesty and integrity can never be emphasized enough, and any violation will be seriously punished. Please get familiar with the rules by checking the following website: <http://www.ust.hk/vpao/integrity/>. Without prior request to the instructor or TA and without proper and verifiable justifications, any absence in courses, debates, or exams will result in zero score for that part in the final score.

1. Assignments (0%). Four to five problem sets will be given, but will not be collected. Students are strongly encouraged to form study groups and work together on each problem set. Solutions will be posted a week after the problem sets are posted, and the TA will go over the solutions in tutorials.

2. Debates (5%+5%). There are two in-class debates on controversial issues about globalization. Each student must choose his/her stand, collectively determine the 4-member debate team that represents him/her, and intellectually support the team. 5% will be lost if his/her team is judged to have lost the debate. More details about the rule will be explained in class. One is on October 20, and the other is on November 26.

3. Exams (25%+40%).

- In-class midterm (October 27, Thursday)
- Final (TBA, but most likely on December 10, Thursday)

4. Short Essay and Critical Review (15%+5%)

- Each student must turn in a short article not exceeding 5 pages (A4 size) on a topic related to this course. Due on November 17, Tuesday.
- Each student will be assigned an anonymous article and must write a 2-page critical review on this article. Due on December 1, Tuesday.
- This CANNOT be directly used for the paper requirement in Econ 367
- These two writing assignments are graded according to the criteria of originality, clarity, conciseness, analytical depth, and writing skills. Both articles and reviews must be typed and turned in both electronic and hard copies. Late essays and reviews are NOT accepted.

5. Class Attendance and Participation in Discussions (5%)

Required Readings

- **Main Textbook:** Paul Krugman and Maurice Obstfeld, *International Economics: Theory & Policy*, 8th edition (2008), Addison-Wesley Publishing Company.
- Lecture Notes
- Papers marked by Asterisks (to be added)

Supplementary Readings (either in library reserve or online)

- Rodrik, Dani, *Has Globalization Gone Too Far?* Institute for International Economics (March 1, 1997).
- Paul Krugman, *The Return of Depression Economics and the Crisis of 2008*. (Hardcover, 2008)
- Joseph Stiglitz, *Globalization and Its Discontent*, 2002.
- Jagdish N. Bhagwati, *In defense of globalization*, 2004

- World Economic Outlook (IMF Publication), 2009
- Useful Websites: [The Economist](#), [WTO](#), [IMF](#), [World Bank](#), [China's Ministry of Commerce](#)

OBE Pilot Course

This course is part of the Outcome Based Education (OBE) Pilot Projects of HKUST. The OBE is a teaching approach that sets clear and specific intended learning outcomes and assesses students' performance based on the planned outcome. For more details, please check the following website: <http://celt.ust.hk/obe/index.htm>.

Tentative Schedule and Topic Objectives (subject to changes)

1. Introduction (1 lecture):

Students should be able to understand the following (Topic Objectives): Economic Globalization: Background, Definition, Measurement, Importance, and Policy Debates.

Readings:

- KO -- Chapters 1, 2, 11.

2. Productivity and Ricardian Trade Models (3 lectures):

Topic Objectives: Productivity, Comparative Advantage, One-Factor Trade Model, Gains from Trade; Patterns of Trade; Firm Heterogeneity

Readings:

- KO -- Chapter 3

3. Endowment and Heckscher-Ohlin Trade Model (3 lectures)

Topic Objectives: Endowment; Two-Factor Trade Model; Factor-Price Equalization; Income Distribution; Developing versus Developed Economies; Structural Change; Industrial Upgrading

Readings:

- KO -- Chapter 4
- Lecture Notes

4. Trade and Income Distribution (2 lectures)

Topic Objectives: Trade and Domestic Income Inequality; Trade and International Wealth Inequality

Readings:

- KO -- Chapters 4, 5, 10, 11
- Lecture Notes

5. Increasing Returns to Scale, Imperfect Competition, and Trade (2 lectures)

Topic Objectives: Economies of Scale; Imperfect Competition; Intra-industry Trade; Externality and Geography

Readings:

- KO -- Chapter 6
- Lecture Notes

6. International Factor Movement (1 lecture)

Topic Objectives: Migration and Capital Flow; Foreign Direct Investment; Multinational Firms; Intra-Firm Trade; Outsourcing

Readings:

- KO – Chapter 7
- Lecture Notes

7. Trade and Growth: Asian Growth-Miracle Economies (2 lectures)

Topic Objectives: Relation between Trade and Growth; Technology Diffusion; Industrial Upgrading; Total Factor Productivity

Readings:

- KO -- Chapters 8-10, Chapter 22.
- Lecture Notes

8: Political Economy of Trade Policies (3 lectures)

Topic Objectives: Instruments of Trade Policies; What Determines Trade Policies; Trade Policy in Developing Economies; World Trade Organization (WTO)

Readings:

- KO -- Chapters 8-10
- Lecture Notes

9. Balance of Payments and Exchange Rates (2 lectures)

Topic Objectives: National Income Accounts, Balance of Payments; Exchanges Rates; Foreign Reserve

Readings:

- KO -- Chapter 12-13.

10. Price Levels and Exchange Rate, Exchange Rate Regimes (2 lectures)

Topic Objectives: Law of One Price; Purchasing Power Parity; Fixed and Floating Exchange Rate Regimes

Readings:

- KO -- Chapters 15, 17, 19.

11. Global Imbalance and Financial Crises (2 lecture)

Topic Objectives: IMF; Financial Market; Global Imbalance; 2008 World Financial Crises; 1998 Asian Financial Crisis

Readings:

- KO – Chapters 18, 21- 22.
- World Economic Outlook 2009

12. Course Review (1 lecture)

More Specific Topic Objectives (subject to changes)

After the lectures, you should be able to

1. Introduction (1 lecture)

- 1.1 Distinguish between international and domestic issues and explain what economic globalization means and how it's measured.
- 1.2 Identify the seven themes that recur in international economics and discuss their importance
- 1.3 Distinguish between the trade and monetary aspects of international economics
- 1.4 Describe the Gravity Model of Trade and discuss its relevance
- 1.5 Describe the general features of the current world trade
- 1.6 Explain why globalization causes many policy debates and identify several most important debates on globalization in the modern time
- 1.7 Describe the role played by China, India, and many East Asian economies in globalization

2. Productivity and Ricardian Trade Models (3 lectures)

- 2.1 Explain how Ricardian Model works and how it illustrates the principle of comparative advantage
- 2.2 Demonstrate gains from trade and refute common fallacies about international trade
- 2.3 Describe the empirical evidence that wage reflect productivity and trade patterns reflect relative productivity
- 2.4 Explain why some firms export while others do not in the same industry and how trade itself affects labor productivity

3. Endowment and Heckscher-Ohlin Trade Model (3 lectures)

- 3.1 Explain how differences in endowment can cause international trade
- 3.2 Discuss and understand why trade affects income distribution; identify who are the losers and who are the winners; explain the gains and losses from the trade for different groups
- 3.3 Discuss why free trade is not widely observed in the real world, although it's economically efficient according to many trade models.
- 3.4 Discuss the implications of the HO Model for the industrial change in the developing economies and the optimal industrial policies for economic development

4. Trade and Income Distribution (2 lectures)

- 4.1 Discuss the relationship between international trade and domestic income inequality both in the short run and in the long run
- 4.2 Discuss why trade may affect the international wealth distribution across different countries both in the short run and in the long run
- 4.3 Discuss how to deal with income distribution in the time of globalization

5. Increasing Returns to Scale, Imperfect Competition, and Trade (2 lectures)

- 5.1 Recognize why international trade often occurs from increasing returns to scale and imperfect competition
- 5.2 Understand the source of intra-industry trade and inter-industry trade; explain their difference
- 5.3 Discuss the role of external economies and knowledge spillover in shaping comparative advantage and trade pattern

6. International Factor Movement (1 lecture)

- 6.1 Discuss the causes and consequences of migration/labor mobility across countries

- 6.2 Understand why multinational firms exist and discuss why FDI is an important phenomenon and describe its general pattern
- 6.3 Discuss why there is a two-way capital flow between the developed and developing economies
- 6.4 Discuss why China and India received starkly different amounts of FDI

7. Trade and Growth: Asian Growth-Miracle Economies (2 lectures)

Topic Objectives: Relation between Trade and Growth; Technology Diffusion; Industrial Upgrading; Total Factor Productivity

- 7.1 Understand TFP and its importance for sustained economic growth
- 7.2 Discuss how trade may affect economic growth and the implications from Asian Growth-Miracle economies
- 7.3 Discuss the effect growth may have on international trade
- 7.3 Discuss: is free trade always good for sustained economic growth?

8: Political Economy of Trade Policies (3 lectures)

Topic Objectives: Instruments of Trade Policies; What Determines Trade Policies; Trade Policy in Developing Economies; World Trade Organization (WTO)

- 8.1 Evaluate the welfare consequences of tariffs, export subsidies and quota policies
- 8.2 Discuss and evaluate the welfare arguments for and against free trade
- 8.3 Discuss the political economy process of trade policy making
- 8.4 Understand the welfare consequence of trade liberalization and the role of WTO
- 8.5 Evaluate the “import-substitution” and “export-orientation” development policies and evaluate the “infant industry” arguments

9. Balance of Payments and Exchange Rates (2 lectures)

- 9.1 Understand the national income accounts in an open economy and the interactions between different components
- 9.2 Describe the balance of payments accounts and understand their relationship to the current account balance, Understand what’s foreign reserve
- 9.3 Understand the meaning of the exchange rate, describe how foreign exchange market functions, and explain what determines the equilibrium exchange rate

10. Price Levels and Exchange Rate, Exchange Rate Regimes (2 lectures)

- 10.1 Understand and explain the law of one price and PPP, discuss the empirical evidence
- 10.2 Understand the difference between fixed and floating exchange rate regimes, both in terms of definitions and how they work
- 10.3 Discuss the pros and cons for the two different regimes
- 10.4 Discuss China’s exchange rate and its impact on trade and growth

11. Global Imbalance and Financial Crises (2 lectures)

- 11.1 Describe the macroeconomic policy goals in an open economy
- 11.2 Understand the background when IMF was established and explain what IMF does
- 11.3 Describe international credit market and international banking and explain why they may need regulations
- 11.4 Discuss how 2008 world financial crisis and 1998 Asian Financial crisis happened and their impacts on the world economy
- 11.5 Discuss what lessons we can learn from the financial crises in developing economies