

18I040

Trade Policy and International Policy Coordination

Winter Term - 3 ECTS

Elective Course

Prof. Giacomo Ponzetto

Prerequisites to Enroll

This elective course builds most directly upon the mandatory course in International Trade and Finance taught by Prof. Jaume Ventura in the Fall Term. The course is focused on formal analysis of theoretical models. The prerequisites to enroll are a good mathematical background (especially on static optimization) and knowledge of game theory at least at the level of an advanced undergraduate course in microeconomics (taking Microeconomics II simultaneously will be helpful).

Overview and Objectives

The growth of long-distance trade and international economic integration have been accompanied by an equally unparalleled level of prosperity for the global economy. Yet, as the downward spiral of world trade between the two world wars vividly testifies, globalization and growth are not immediate and automatic consequences of technological progress. On the contrary, a flourishing interconnected world economy relies crucially on political institutions. Governments need to create the physical and regulatory infrastructure that underpins commerce and market integration, and to refrain instead from destructive protectionist policies. Globalization thus represents a governance challenge.

The goal of this course is to use the tools of trade theory and political economics to understand this challenge and the development of international institutions and rules for policy coordination. We will consider first trade policy in the narrow sense of protectionist trade barriers. We will examine the political motives driving their adoption, both internationally to manipulate the terms of trade and domestically to redistribute the gains from trade to politically favored groups. We will then study the role of the World Trade Organization as a mechanism to achieve Pareto-improving multilateral trade liberalization. We will move on to consider how globalization has spurred political integration in a broader sense, from the formation of large countries and colonial empires after the Industrial Revolution to the creation of international unions during the last few decades. We will analyze the political determinants of membership in international unions and of union-wide policy, with a particular focus on monetary and fiscal unions.

Course Outline

1. The basic theory of trade policy
2. The political economy of trade policy

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3. Trade agreements and the World Trade Organization
4. Trade and political geography: the rise of international unions
5. Monetary unions
6. Fiscal unions

Required Activities

Class participation.

Evaluation

Students will be evaluated through a written exam at the end of the course.

Competences

- To (be able to) communicate with determination and in the English Language, the results and implications of the required analytical study using a language that the receiver can relate to.
- To fit in diverse professional environments and varied types of collaborations in different professional projects
- To possess and understand the knowledge that provides a basis or opportunity to be original in the development and / or application of ideas, often in a research context.
- That students know how to apply the acquired knowledge and their ability to solve problems in new or unfamiliar environments within broader (or multidisciplinary) contexts related to their field of study.
- That the students be able to integrate knowledge and face the complexity of making judgments based on information that, being incomplete or limited, include reflections on the social and ethical responsibilities linked to the application of their knowledge and judgments.
- That the students be able to communicate their conclusions and the knowledge and the ultimate reasons that sustain them to both, specialized and non-specialized publics in a clear and unambiguous way.
- That students possess the learning skills that allow them to continue studying in a way that will be largely self-directed or autonomous.

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- To identify and apply the insights of the theory, the models, and the analytical tools of modern economy to its global dimension.
- Understand and apply economic theory related to the regulation of markets and competition policy.
- Understand and apply the economics of international trade and finance and economic development
- To evaluate, with theoretical and quantitative instruments, the complex realities of the economy to understand the way it works.

Learning Outcomes

- Deep knowledge of the economics of international trade, finance and development.
- Applies economic concepts to economic pressure policy problems related to growth, economic stability and poverty.

Materials

For all topics, class slides are the main reading. The following is a list of suggested further readings.

1. The Basic Theory of Trade Policy

This topic is covered in the slides and in any textbook. The following textbook is freely available online:

Markusen, J., J. Melvin, W. Kaempfer and K. Maskus (1995). *International Trade: Theory and Evidence*
<http://spot.colorado.edu/~markusen/textbook.html>

A useful introductory reference to international trade and trade policy is the following:

WTO (2008). *World Trade Report 2008 – Trade in a Globalizing World*
https://www.wto.org/english/res_e/booksp_e/anrep_e/world_trade_report08_e.pdf
https://www.wto.org/english/res_e/booksp_e/anrep_e/world_trade_report08_e.pdf

The following readings are cited in the slides, but only as background information:

Bhagwati, J.N. (1971). "The Generalized Theory of Distortions and Welfare." In: J. Bhagwati et al., eds., *Trade, Balance of Payments and Growth* (North-Holland).

Dixit, A. K. (1987). "Strategic Aspects of Trade Policy." In: T. Bewley, ed., *Advances in Economic Theory* (Cambridge University Press).

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2. The Political Economy of Trade Policy

The class slides cover extensively four papers:

Grossman, G.M., and E. Helpman (1994). "Protection For Sale." *American Economic Review*, 84(4): 833–850.

Goldberg, P. Koujianou, and G. Maggi (1999). "Protection for Sale: An Empirical Investigation." *American Economic Review*, 89(5): 1135–1155.

Dutt, P., and D. Mitra (2002). "Endogenous Trade Policy through Majority Voting: An Empirical Investigation." *Journal of International Economics*, 58(1): 107–133.

Enikolopov, R., M. Petrova and G.A.M. Ponzetto (2019). "The Dracula Effect: Voter Information and Trade Policy." Mimeo, Universitat Pompeu Fabra.

Note: An earlier version of this paper circulated as CEPR Discussion Paper 8726 "Heterogeneous Information and Trade Policy." However, the empirical section of this Discussion Paper is superseded and is not recommended reading.

Two more articles are briefly summarized in the class slides:

Bombardini, M. (2008). "Firm Heterogeneity and Lobby Participation." *Journal of International Economics*, 75: 329–348.

Mitra, D. (1999). "Endogenous Lobby Formation and Endogenous Protection: A Long-Run Model of Trade Policy Determination," *American Economic Review*, 89(5): 1116–1134.

The following readings are cited in the slides, but only as background information:

Ansolabehere, S., J.M. de Figueiredo, and J.M. Snyder (2003). "Why Is There So Little Money in U.S. Politics?" *Journal of Economic Perspectives*, 17(1): 105–130.

Bernheim, D.B., and M.D. Whinston (1986). "Menu Auctions, Resource Allocation, and Economic Influence." *Quarterly Journal of Economics*, 101: 1–31.

Bhagwati, J.N. (1988). *Protectionism* (MIT Press).

Eicher, T., and T. Osang (2002). "Protection for Sale: An Empirical Investigation: Comment." *American Economic Review*, 92: 1702–1710.

Eisensee and Strömberg (2007). "News Droughts, News Floods and U.S. Disaster Relief." *Quarterly Journal of Economics*, 122(2): 693–728.

Findlay, R., and S. Wellisz (1982). "Endogenous Tariffs, the Political Economy of Trade Restrictions, and Welfare." In: J.N. Bhagwati, ed., *Import Competition and Response* (University of Chicago Press).

Gawande, K., and U. Bandyopadhyay (2000). "Is Protection for Sale? Evidence on the Grossman-Helpman Theory of Endogenous Protection." *Review of Economics and Statistics*, 82: 139–152.

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- Gawande, K., P. Krishna and M. Olarreaga (2009), "What Governments Maximize and Why: The View from Trade." *International Organization*, 63: 491–532.
- Grossman, G.M., and E. Helpman (1996). "Electoral Competition and Special Interest Politics." *Review of Economic Studies*, 63: 265–286.
- Hall, H.K., C. Kao and D. Nelson (1998). "Women and Tariffs: Testing the Gender Gap Hypothesis in a Downs-Mayer Political-Economy Model." *Economic Inquiry*, 36: 320–332.
- Hillman, A.L. (1982). "Declining Industries and Political-Support Protectionist Motives." *American Economic Review*, 72: 1180–1187.
- Kee, H.L., A. Nicita and M. Olarreaga (2008). "Import Demand Elasticities and Trade Distortions." *Review of Economics and Statistics*, 90: 666–682.
- Kee, H.L., A. Nicita and M. Olarreaga (2009). "Estimating Trade Restrictiveness Indices." *Economic Journal*, 119: 172–199.
- Levitt, S.D. (1994). "Using Repeat Challengers to Estimate the Effect of Campaign Spending on Election Outcomes in the U.S. House." *Journal of Political Economy* 102(4): 777–798.
- Long, N.V., and N. Vousden (1991). "Protectionist Responses and Declining Industries." *Journal of International Economics*, 30: 87–103.
- Magee, S.P., W.A. Brock and L. Young (1989). *Black Hole Tariffs and Endogenous Policy Theory* (Cambridge University Press).
- Matschke, X., and S.M. Sherlund (2006). "Do Labor Issues Matter in the Determination of U.S. Trade Policy? An Empirical Reevaluation." *American Economic Review*, 96: 405–421.
- Mayda, A.M., and D. Rodrik (2005). "Why Are Some People (and Countries) More Protectionist than Others?" *European Economic Review*, 49: 1393–1430.
- Mayer, W. (1984). "Endogenous Tariff Formation," *American Economic Review*, 74: 970–985.
- McCalman, P. (2004). "Protection for Sale and Trade Liberalization: an Empirical Investigation." *Review of International Economics*, 12(1): 81–94.
- Mian, A., A. Sufi, and F. Trebbi (2010). "The Political Economy of the US Mortgage Default Crisis." *American Economic Review*, 100(5): 1967–1998.
- Mitra, D., D.D. Thomakos and M.A. Ulubaşoğlu (2002). "'Protection for Sale' in a Developing Country: Democracy vs. Dictatorship." *Review of Economics and Statistics*, 84: 497–508.
- Mitra, D., D.D. Thomakos and M.A. Ulubaşoğlu (2006). "Can we obtain realistic parameter estimates for the 'protection for sale' model?" *Canadian Journal of Economics*, 39: 187–210.
- Persson, T., and G. Tabellini (2000). *Political Economics* (MIT Press).

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Rodrik, D. (1995). "Political Economy of Trade Policy." In: G.M. Grossman and K. Rogoff, eds., *Handbook of International Economics*, vol. 3 (North-Holland).

Stigler, G.J. (1971). "The Theory of Economic Regulation." *Bell Journal of Economics and Management Science*, 2: 3–12.

Strömberg, D. (2004). "Radio's Impact on Public Spending." *Quarterly Journal of Economics*, 119: 189–221.

Trefler, D. (1993). "Trade Liberalization and the Theory of Endogenous Protection: An Econometric Study of U.S. Import Policy." *Journal of Political Economy*, 101: 138–160.

3. Trade Agreements and the World Trade Organization

The class slides follow closely a seminal article and its book-length extension:

Bagwell, K. and R. Staiger (1999). "An Economic Theory of GATT." *American Economic Review*, 89: 215–248.

Bagwell, K. and R. Staiger (2002). *The Economics of the World Trading System* (MIT Press).

The following readings are cited in the slides, but only as background information:

Chang, W., and L.A. Winters (2002). "How Regional Blocs Affect Excluded Countries: The Price Effects of MERCOSUR." *American Economic Review*, 92(4): 889–904.

Kemp, M.C., and H.Y. Wan (1976). "An elementary proposition concerning the formation of customs unions." *Journal of International Economics*, 6(1): 95–97.

Winters, L.A., and W. Chang (2000). "Regional integration and import prices: an empirical investigation." *Journal of International Economics*, 51(2): 363–377.

4. Trade and Political Geography: The Rise of International Unions

The class slides cover extensively two articles:

Gancia, G., G.A.M. Ponzetto and J. Ventura (2018). "Globalization and Political Structure." CEPR Discussion Paper 11159.

Alesina, A., I. Angeloni and F. Etro (2005). "International Unions." *American Economic Review*, 95(3): 602–615.

The following readings are cited in the slides, but only as background information:

Alesina, A., and E. Spolaore (1997). "On the Number and Size of Nations." *Quarterly Journal of Economics*, 112(4): 1027–1056.

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Alesina, A., and E. Spolaore (2003). *The Size of Nations* (MIT Press).

Anderson, J.E., and E. van Wincoop (2004) "Trade Costs." *Journal of Economic Literature*, 42(3):691–751.

McCallum, J. (1995). "National Borders Matter: Canada–U.S. Regional Trade Patterns." *American Economic Review*, 85(3): 615–623.

Oates, W.E. (1972). *Fiscal Federalism* (Harcourt Brace Jovanovich).

5. Monetary Unions

The class slides follow closely a seminal article:

Alesina, A., and R.J. Barro (2002). "Currency Unions." *Quarterly Journal of Economics*, 107(2): 409–436.

One more article is briefly summarized in the class slides:

Mundell, R.A. (1961). "A Theory of Optimum Currency Areas." *American Economic Review*, 51(4): 657–665.

6. Fiscal Unions

The class slides cover extensively two articles:

Persson, T., and G. Tabellini (1996a). "Federal Fiscal Constitutions: Risk Sharing and Moral Hazard." *Econometrica* 64(3): 623–646.

Persson, T., and G. Tabellini (1996b). "Federal Fiscal Constitutions: Risk Sharing and Redistribution." *Journal of Political Economy* 104(5): 979–1009.