

STELLENBOSCH UNIVERSITY

Economics 771 – Second Semester 2022

International Trade Theory and Policy

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1. COURSE OBJECTIVE

The act of exchange underpins all of economics. Trade which crosses international borders is a simple extension of this principle. In this course we will consider the three major 'waves' of theories used to explain trade between countries, industries and firms, and the empirical evidence which led to major theoretical advances in trade theory.

By the end of the course, the successful students should:

- Understand different theoretical explanations for why countries, industries and firms engage in international trade.
- Discuss the assumptions which underlie these different theories and thus determine when they are appropriate tools for understanding trade.
- Be familiar with the main empirical work which led to the development of these theories and/or provides support for them.
- Have better understanding of why countries trade, who benefits and loses and what trade policies are appropriate for different developing countries such as Lesotho, South Africa, Zambia and Kenya
- Have gained experience in applying their quantitative (econometric and economic tools) and analytical skills to real world situations.

2. COURSE DESIGN AND LECTURES

Formal lectures: Wednesdays 10:00 - 13:00 (CGW Schumann Building Room 221)

Practical/tutorial sessions: Tuesdays 10:00 - 13:00 (CGW Schumann Building Room 221)

We consider all three parts to be vital in the training of an economist; therefore, satisfactory performance in *each* part is required to pass (see **Course Evaluation**).

The lectures make liberal and frequent use of the standard tools of microeconomics and mathematical optimization which were covered in the microeconomics and mathematics courses. Some attention will be given to many of the microeconomics features, but elements like producer theory results will be taken as known and mastered by the student.

Students are expected to engage in critical and logical thinking, and to work towards developing concise and rigorous reasoning and writing skills. The course places great emphasis on active and extensive practice in problem solving as well as in-class participation during discussions. All these elements will be assessed.

3. COURSE EVALUATION

Assessment will be based on a mid-term test, practical assignment, an essay, class presentations and a class participation mark. Assessments count as follows:

Evaluation	Weight in final Mark	Date
Class presentations	15%	
Tutorial Sessions	20%	Due before or in Tutorial Class
Mid-term Exam	40%	Wednesday, 19 October 2022 (10am-1pm)
Course Essay	25%	Due Friday, 23 September 2022 (midnight)

Trade seminars

The objective of the seminar is for students to engage in detailed discussions on a particular topic. Each of these topics poses challenges to trade theory as they are covered in each section of the course. Students are expected to draw on the relevant literature and provide key insights, drawing reference to the existing theory that would have already been covered. Students are encouraged to present an integrated analysis, as opposed to a presentation of each paper separately. To help students, certain key questions have been identified around which they may wish to structure their presentations.

Grading will be awarded for the seminar presentations and discussions- This will motivate students to present a good story and *reasonably* contribute to the discussions of other presentations. Each presentation should consist of no more than 20 slides and take no more than half an hour. In each case, students are encouraged to draw implications for Africa.

Tutorials sessions and problem sets

Problem Sets will be assigned during the course and are due to be handed in for grading **on or before the next tutorial session**. The tutorials are intentionally challenging and will in many cases apply methods introduced in lectures to more complicated cases than those covered in the lectures, for students to develop problem solving skills and a deeper understanding of the methodology used in trade theory.

Students are encouraged to work together in groups on the problem sets, but each student will hand in his/her own work and copying answers is not allowed. Students that rely too much on the group without ensuring that they can solve the same kinds of problems independently may struggle in the main assessments (essay, practical assignment, and mid-term exam).

Course Essay

The requirements are:

- The TurnItIn.com submission must be the final, **complete** essay in **pdf** form, with *all* headings, citations, figures, tables and references. The code is:
- 12pt font, **2 line spacing** (this makes it easier to do inline comments on TurnItIn.com)
- A plagiarism declaration must be completed. Do not rely on the turnitin.com “score” to judge whether an essay contains plagiarism or not. It is each student’s responsibility to fully understand what may be regarded as plagiarism and to ensure that there is no plagiarism in his/her essay. Plagiarism is a serious offense with serious consequences and very little (if any) leniency can be expected at postgraduate level.

- The word limit for this essay is 2000, excluding title page and references. This maximum will be strictly enforced: word limit penalties will be applied proportional to the number of words exceeding 2000. Please report your word count on the title page of your essay.
- A late submission penalty of 2 percentage points per day late will be imposed.

Marks are allocated according to how well students perform in terms of content, structure, use of sources, writing style and technical matters.

Criteria for passing course:

To pass the course a student must have:

- A Final Course Mark of at least 50%
- and**
- A main assessment (mid-term exam) mark of at least 40%

4. READINGS

There is no prescribed textbook for the course. Material will be drawn from a range of sources including textbooks, academic articles and reports and class notes.

Main Textbooks

Feenstra, Robert C (2016), *Advanced International Trade: Theory and Evidence* Princeton University Press.

Markusen, James R., J.R. Melvin, William H. Kaempfer and Maskus (1995), *International Trade: Theory and Evidence*. New York: McGraw Hill.

<http://spot.colorado.edu/~markusen/textbook.html>

Recommended Textbooks

Bowen, H.P., A. Hollander, and J. Viaene (2012), *Applied International Trade Analysis*, 2nd Edition, London, Macmillan Ltd.

Caves, Frankel R.E., Jeffrey A. and Ronald W. Jones (2017), *World Trade and Payments: An Introduction*, 10th Edition, London: Addison-Wesley (forthcoming).

Feenstra, R. and Taylor, A.M. (2021) *International Economics*, 5th edition. Macmillan.

Husted, S. And Melvin, M. (2013), *International Economics*, 9th edition, Pearson.

Krugman, P., Obstfeld, M, Melitz, M. (2018), *International Economics: Theory and Policy*, Global edition, 11th edition Pearson Education.

Major Website Resources

(a) Joint World Bank and International Monetary Fund External Libraries (JOLIS)

<http://jolis.worldbankimflib.org/external.htm>

(b) WEbEC WWW-Resources in Economics: <http://wwhelsinki.fi/WebEc/WebEc.html>

(c) Social Science Research Network eLibrary: <http://ww.ssrn.com/>

(d) Eldis Trade Policy Resource Guide: <http://www.eldis.org/trade/index.htm>

(e) Gravity Database: (<http://www.cepii.fr/>)

(f) Direction of Trade Statistics (IMF)

(g) World Integrated Trade Solutions (WITS) database (<http://wits.worldbank.org>)

5. COURSE CONTENT (12 WEEKS)

We will cover a selection of the following topics during the semester. Any deviations from the course outline will be announced during class, or via SUNlearn. The list of readings provided is provisional and will be updated on the website.

INTRODUCTION TO INTERNATIONAL TRADE (1 week)

What is international trade? Why is it important to study international trade?

PART A: PERFECT COMPETITION MODELS OF TRADE (3 Weeks)

1. Theories of comparative advantage: Ricardo model (1 week)

What is comparative advantage? How does comparative advantage differ from competitive advantage? How well does the Ricardo model explain trade flows?

Readings

Feenstra (2016), Ch. 1

Markusen, Melvin, Kaempfer & Maskus (1995), Ch.8.

Golub, S. and Edwards, L. (2004) "South Africa's International Cost Competitiveness and Productivity in Manufacturing," *World Development*, 32, 8: 1323-1339.

2. Factor Endowments and the Heckscher-Ohlin model (1 week)

How do factor endowments affect trade flows? Is the HO theorem supported by empirical evidence?

Readings

Feenstra (2016) Ch. 2 & 3

Markusen, Melvin, Kaempfer & Maskus (1995), Ch.9.

Davis, D. and D. Weinstein, (2003) "The Factor Content of Trade", in E.K. Choi and J. Harrigan (eds.) *Handbook of International Trade*, Oxford: Basil Blackwell (NBER Working Paper No. 8637)

3. Empirical Evidence & Applications to Africa: Trade seminar (1 week)

How does Africa's labour cost competitiveness compare with other developing countries? Is HO theorem supported by empirical evidence from Africa?

Reading

Wood, A. and Mayer, J. (2001) "Africa's Export Structure in a Comparative Perspective," *Cambridge Journal of Economics*, 5(3): 369-394.

PART B: NEW TRADE THEORIES (3 WEEKS)

1. Imperfect (Monopolistic) Competition Models of Trade (1 week)

Readings

Markusen, Melvin, Kaempfer & Maskus (1995), Ch. 11, 12, 13 and 14.

Feenstra (2016), Ch.5 & 6.

Helpman, E. (1984) "Increasing Returns, Imperfect Markets, and Trade Theory," in Jones, R.W. and Hummels, D. and J. Levinsohn (1995), "Monopolistic Competition and International Trade: Reinterpreting the Evidence," Quarterly Journal of Economics, 110, 799-836. Page 5 of 16
Krugman, P. (1991) "Increasing returns and Economic Geography", Journal of Political Economy, 99(3), 483-499.

2. Distance and the Gravity Equation (1 week)

Distance effects on bilateral trade are one of the "clearest and most robust empirical findings in economics" Leamer and Levinsohn (1994).

There is a common belief that Africa trades "too little" both with itself and the rest of the world. In 1990 intraregional trade shares for Africa were 4 percent compared with 44 percent for East Asia (Frankel, 1997).

Analysis of African trade flows indicates that their relatively low level is largely due to poor infrastructure (Limao and Venables, 2001)

In this session we use gravity models to empirically evaluate the above statements.

Readings

Anderson, J.E. and E. van Wincoop (2003), "Gravity with Gravitas: a Solution to the Border Puzzle", The American Economic Review, 93, 170-192.

McCallum, John. 1995. "National Borders Matter." American Economic Review 85:615-23

3. Empirical Evidence & Applications to Africa: Trade seminar (1 week)

Readings

Didia, D., Nica, M. & Yu, G. (2015) "The gravity model, African growth, and opportunity Act (AGOA), and US trade relations with Sub-Saharan Africa." The Journal of International Trade and Economic Development, volume 24 (8), 1130-1151.

RECESS (1 WEEK)

PART C: TRADE AND FIRMS (2 Weeks)

1. General Surveys and Empirical Evidence from Firm and Plant Data (1 week)

Are the stylized facts about firm and product level trade consistent with trade theory? Do exporters differ from firms that produce for domestic markets? How concentrated is trade? Are African firms different? Does firm-level analysis support theoretical predictions? What determines the exporter-productivity relationship? Why can't you trust trade relationships using aggregate data?

Readings

Bernard, A. B., Redding, Stephen J. and Peter K. Schott, (2007) "Firms in International Trade," Journal of Economic Perspectives, 21(3),105-130.

Melitz, M.J. (2003) "The Impact of Trade on Intra-Industry Reallocations and Aggregate Industry Productivity," Econometrica, 71 (6): 1695-1725.

2. Empirical Evidence & Applications to Africa: Trade Seminar (1 week)

Readings

Rankin, N., M. Söderbom and F. Teal (2006) “Exporting from manufacturing firms in sub-Saharan Africa”, *Journal of African Economies*, 15(4), December, 671-687.

PART D: INTERNATIONAL TRADE POLICY (2 WEEKS)

1. Analysis of tariff and non-tariff barriers (1 week)

Instruments of Intervention, their Effects and Measurement: Tariff and Non-Tariff Barriers. Strategic Trade Policy. Political Economy of Trade Policy. Economic Integration: Prospects of Regional Integration in Africa; Constraints, Conflicts, and Challenges of Regional Integration in Africa. AfCFTA.

Readings

Markusen, Melvin, Kaempfer & Maskus (1995), Ch. 15, 16, 17, 18, 19 and 20.

Feenstra (2016), Ch. 7, 8, 9, & 10.

Byiers, B., Apiko, P., & Karkare, P. (2021). The AfCFTA and industrialisation.

Leshoele, M. (2020). AfCFTA and Regional Integration in Africa: Is African Union Government a Dream Deferred or Denied? *Journal of Contemporary African Studies*, 1–15

2. Empirical Evidence & Applications to Africa: Trade Seminar (1 week)

Readings

Stern, M. and Y. Ramkolowan (2021) “Understanding South Africa’s Trade Policy and Performance”, SARB working Paper.

PART E: TRADE AND ECONOMIC DEVELOPMENT (2 WEEK)

1. Trade, industrialisation, and development (1 week)

Readings

Dollar, D. and Kraay, A. (2004) “Trade, Growth and Poverty.” *The Economic Journal*, 114: F22-F49.

Black, A., Edwards, L., Ismail, F., Makundi, B., & Morris, M. (2021). The role of regional value chains in fostering regional integration in Southern Africa. *Development Southern Africa*, 38(1), 39-56.

Levin, S., & Makgetla, N. (2021). Regional value chains and industrialisation: The southern African experience. *Transforming agriculture: Harnessing regional value chains and industrial policy for development*, 1-30.

1. Empirical Evidence & Applications to Africa: Trade Seminar (1 week)

Readings

Avom, D., Tiako, I., & Nguenkeng, B. (2021). Regional Value Chains and Industrialization of Sub-Saharan Africa. *Theoretical Economics Letters*, 11(6), 1312-1327.

<i>Week</i>	Tuesday 10:00	Wednesday 10:00	Other
1	No Tutorial	20 July Lecture 1: Introduction to International Trade	
2	No Tutorial	27 July Lecture 2: Ricardo model	
3	2 August Tutorial 1	3 August Lecture 3: H-O Model	
4	9 August Public Holiday	10 August Lecture 4: Trade Seminar	
5	16 August Tutorial 2	17 August Lecture 5: New Trade Theories	
6	23 August Tutorial 3	24 August Lecture 6: Gravity Model	
7	30 August Tutorial 4 (Practical session)	31 August Lecture 7: Trade Seminar	
8	Recess	Recess	Recess
9	No tutorial	14 September Lecture 8: Trade and Firms	
10	No tutorial	21 September Lecture 9: Trade Seminar	Friday, 23 September Essay Submission
11	27 September Practical Tutorial 5	28 September Lecture 10: International Trade Policy	
12	4 October Tutorial 6	5 October Lecture 11: Trade and Development	
13	11 October Tutorial 7	12 October Lecture 12: Trade Seminar	
14		19 October Mid-Term Exam	

Schedule: Dates for Lectures and Tutorials

END!!