

Econ 340

Lecture 1

Overview of the World Economy

Announcements

- We will start discussing news next week, on Monday Sep 16. You should be watching now for international economic news.
- Be sure to register your clicker on the Canvas site for this course.
- I will not be holding my usual office hour this Thursday, Sep 12.

Clicker Question

Are you here?

- ✓ a) Yes
- b) No
- c) I'm not sure

Lecture 1 Outline

Overview of the World Economy

- “Globalization”
- Elements of the World Economy
- Ways that Countries Interact
 - Trade
 - Capital Flows
 - Migration
- Policies that Affect Others
- Institutions

Overview of the World Economy

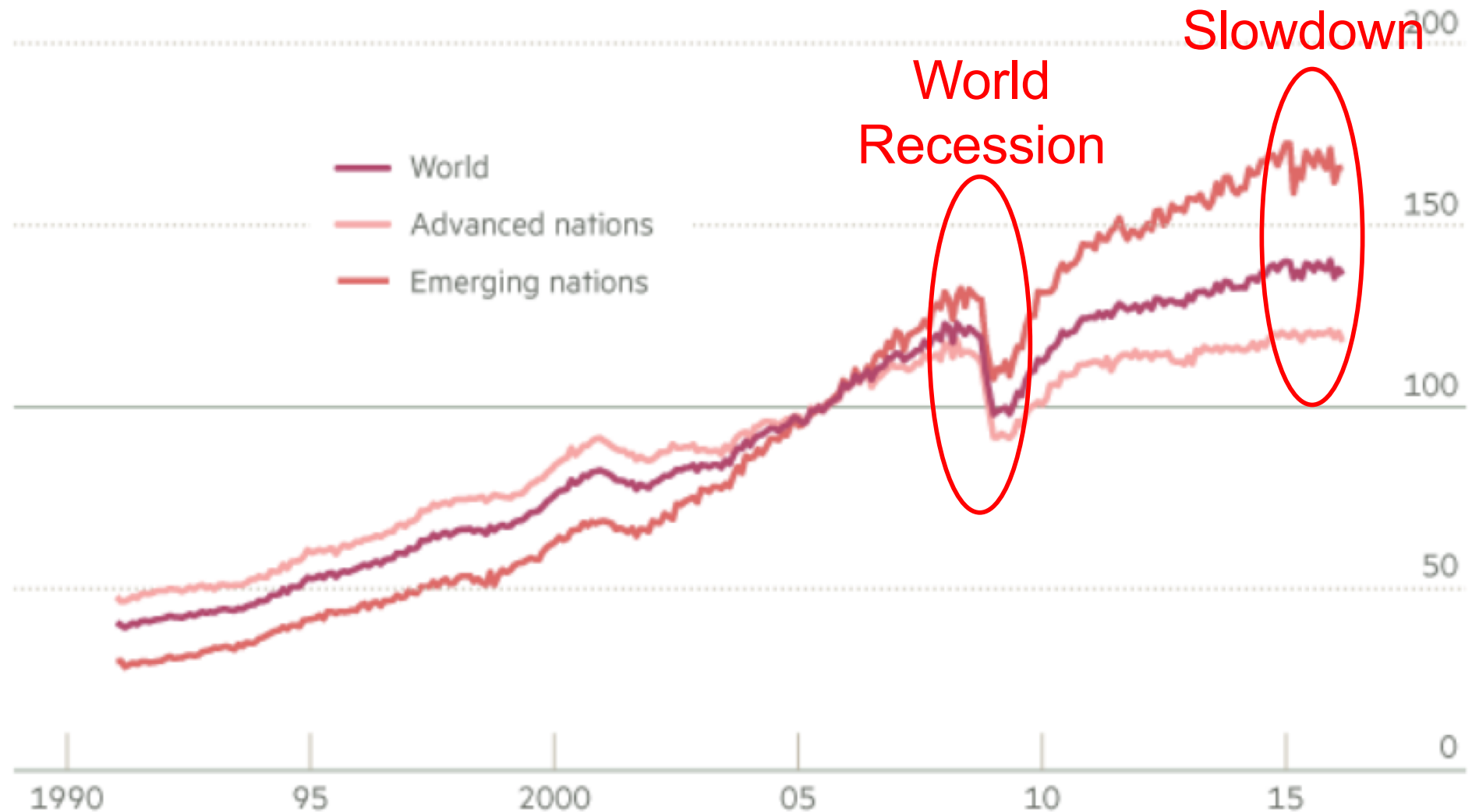
- “Globalization”
 - Means different things to different people
 - My definitions (see my online Glossary):
 1. The increasing world-wide integration of markets for goods, services and capital.
 2. Also the role of MNCs, IMF, WTO, World Bank.
 3. Elsewhere: domination by United States.
 - Some see good, others see bad

Overview of the World Economy

- “Globalization”
 - Some aspects of globalization, especially trade,
 - Declined with the world recession of 2008, then recovered
 - Slowed down in 2015-16
 - Resumed growth in 2017
 - What’s next? We don’t know!

World trade plateaued around the start of 2015

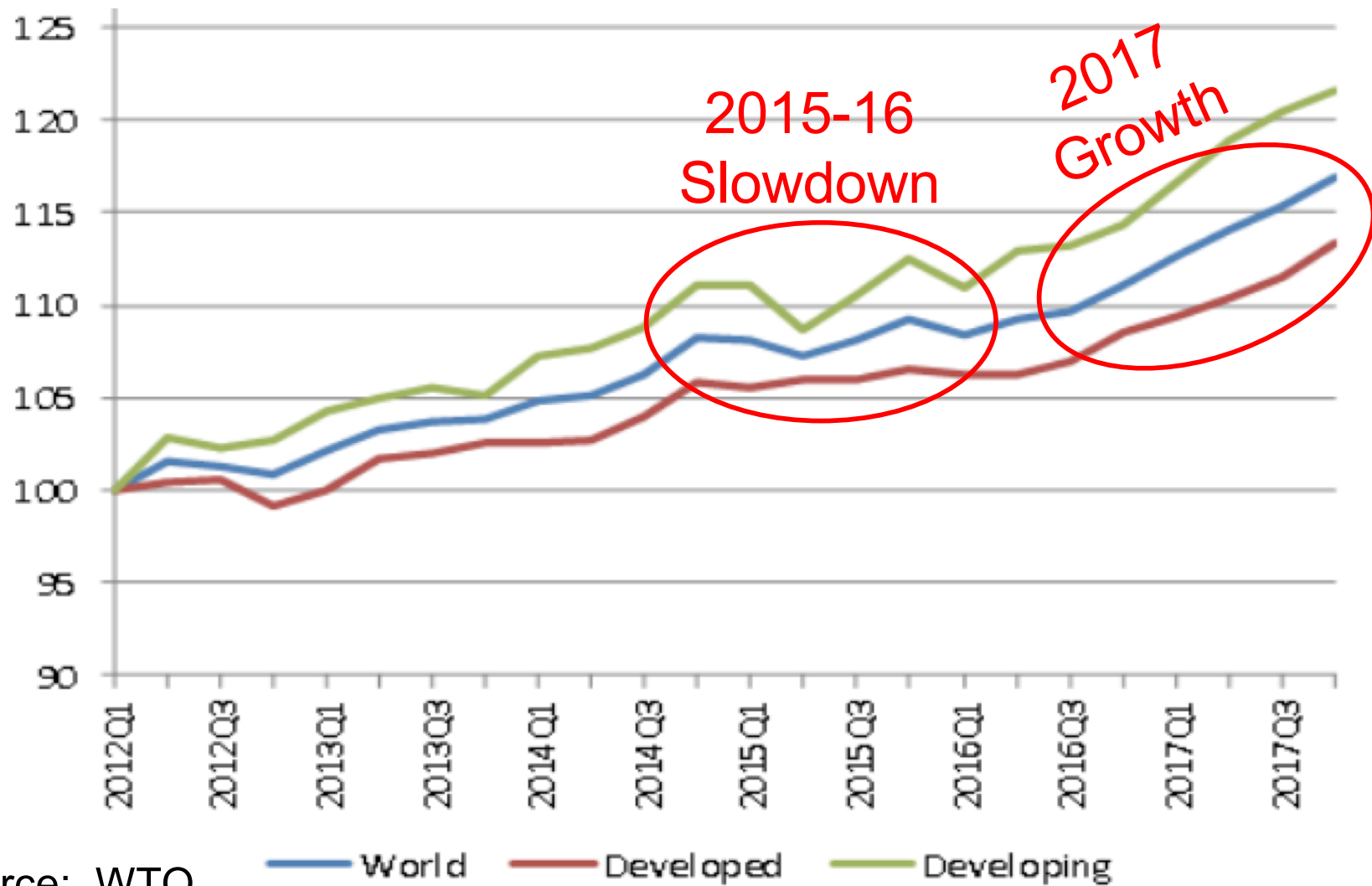
Export volume index (2005=100)



Source: Centre for Economic Policy Research

FT

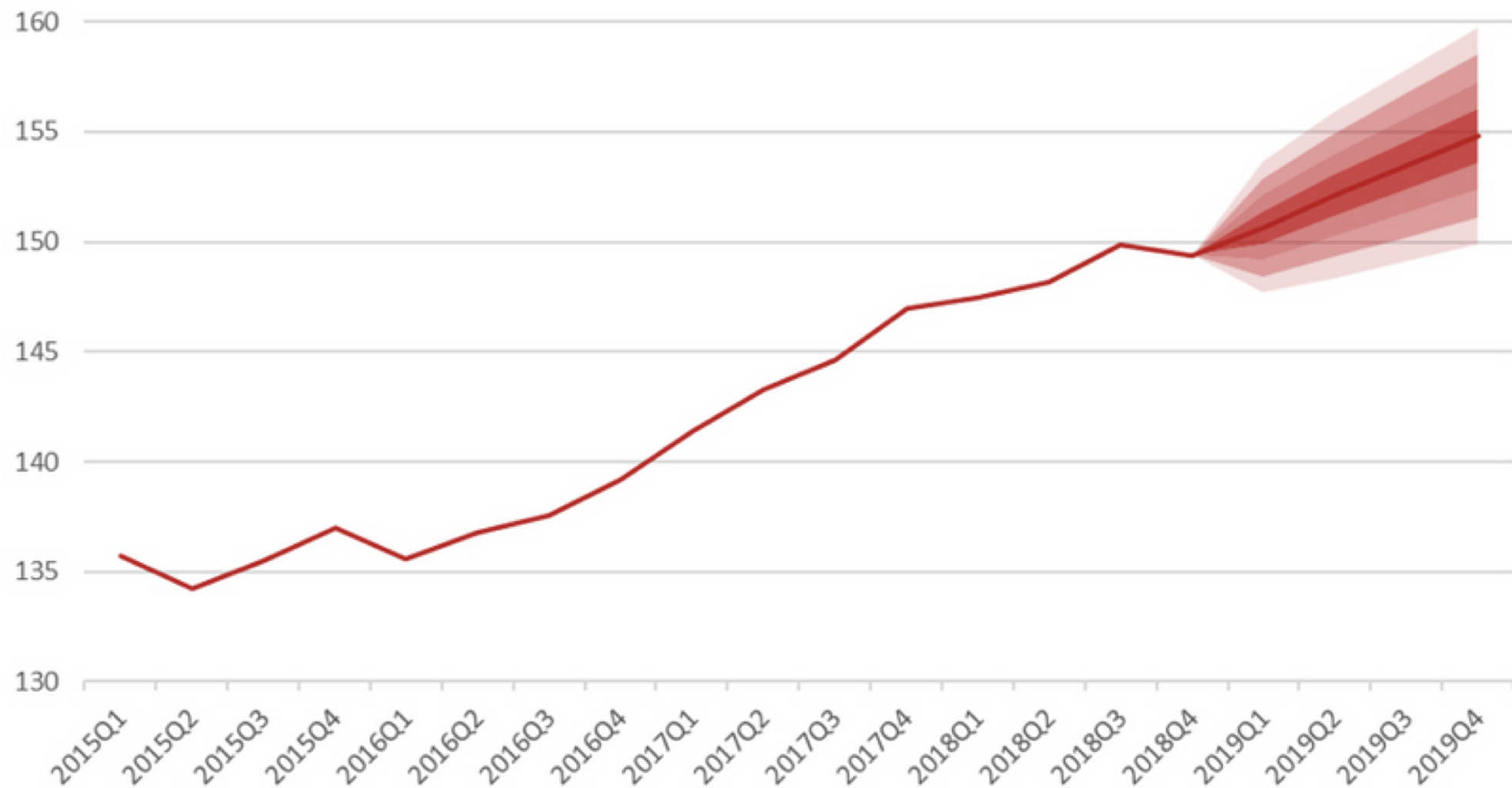
World Merchandise Exports by Level of Development, 2012Q1 – 2017Q4 (Volume index, 2012Q1=100)



Source: WTO

Chart 2: Volume of world merchandise trade, 2015Q1-2019Q4

Seasonally-adjusted volume index, 2005=100



Source: WTO and UNCTAD, WTO Secretariat estimates.

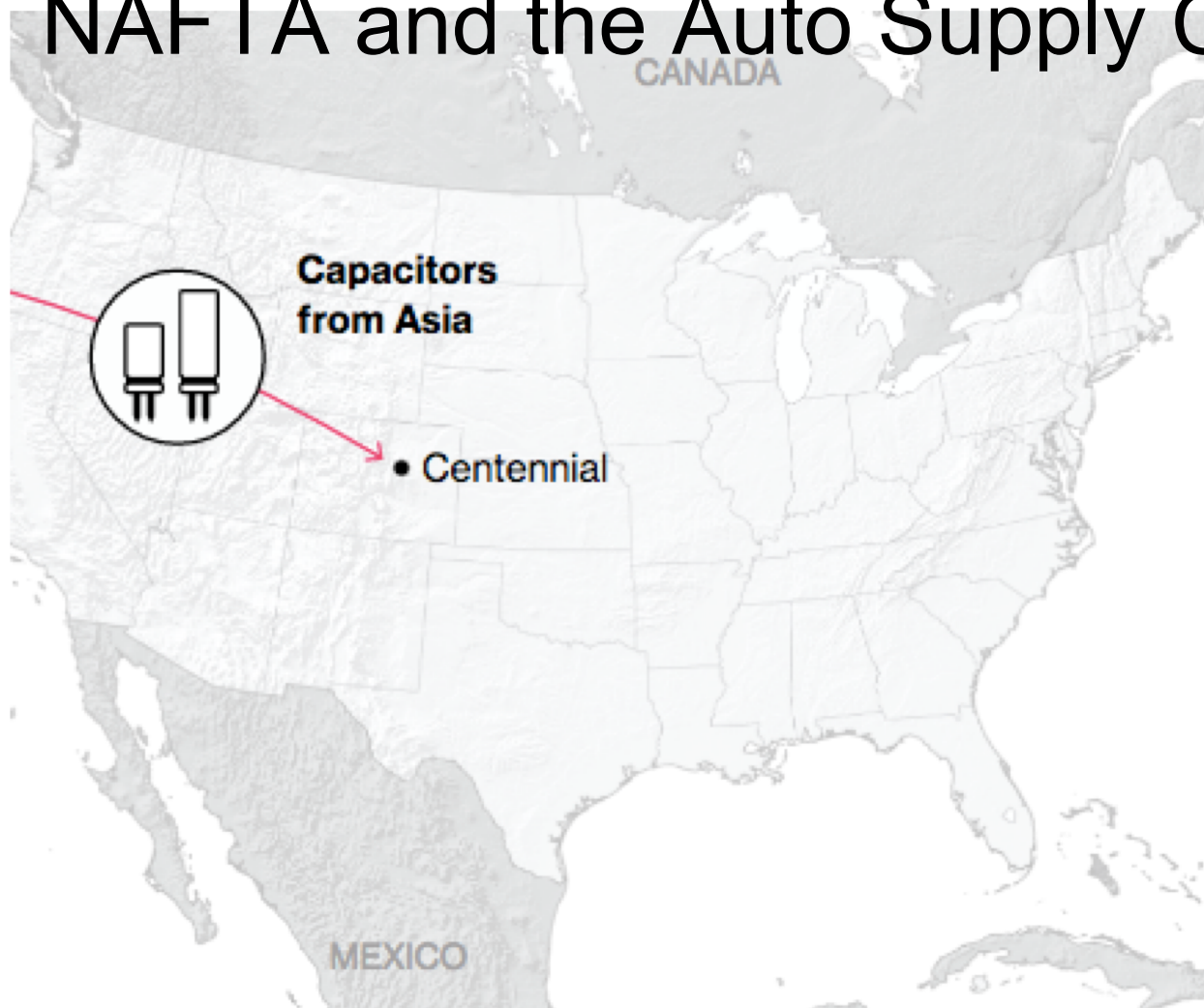
Overview of the World Economy

- Globalization Backlash
 - There is growing opposition to globalization
 - This happened before, with the “First Globalization” (See Swanson)
 - Both trade and migration grew strongly up to World War I in 1914
 - Inequality also grew
 - Trade and migration both declined for decades after

Globalization of Supply Chains

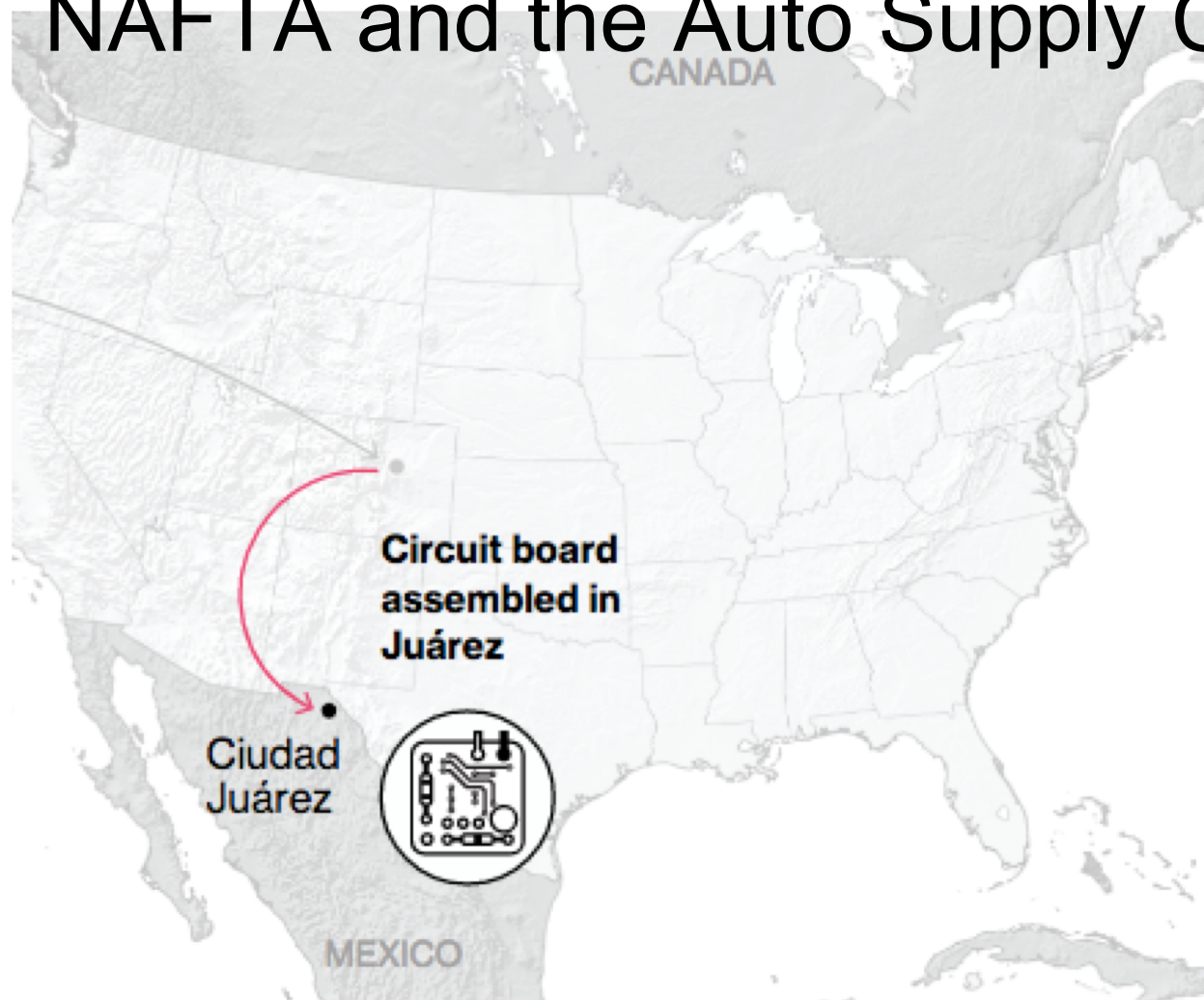
- Much trade today is intermediate inputs.
- Supply chains cross national borders multiple times
- Example from Black

NAFTA and the Auto Supply Chain



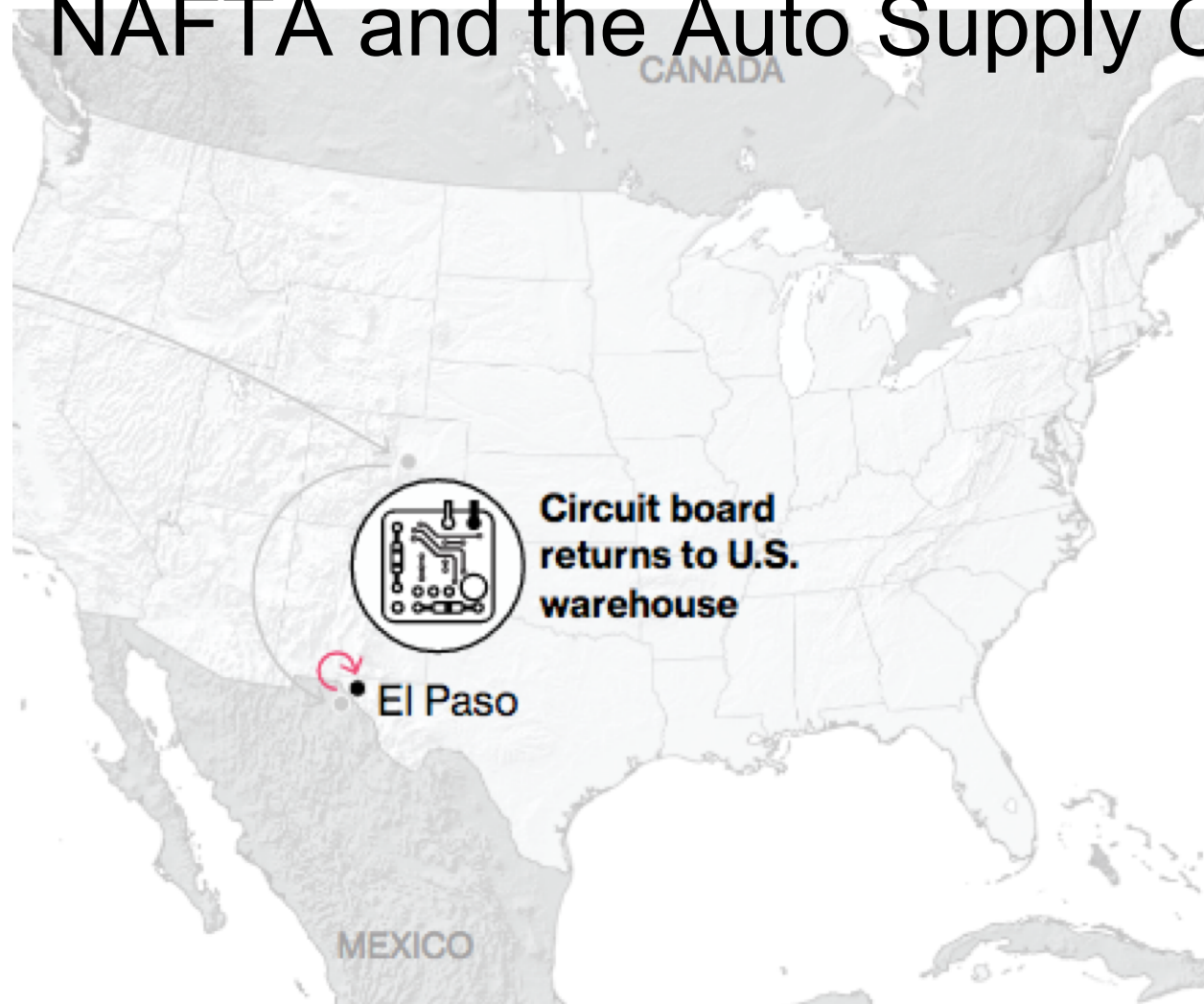
Black, Diamond, and Merrill, “One Tiny Widget’s Dizzying Journey Shows Just How Critical Nafta Has Become,” *Bloomberg*, February 2, 2017.

NAFTA and the Auto Supply Chain



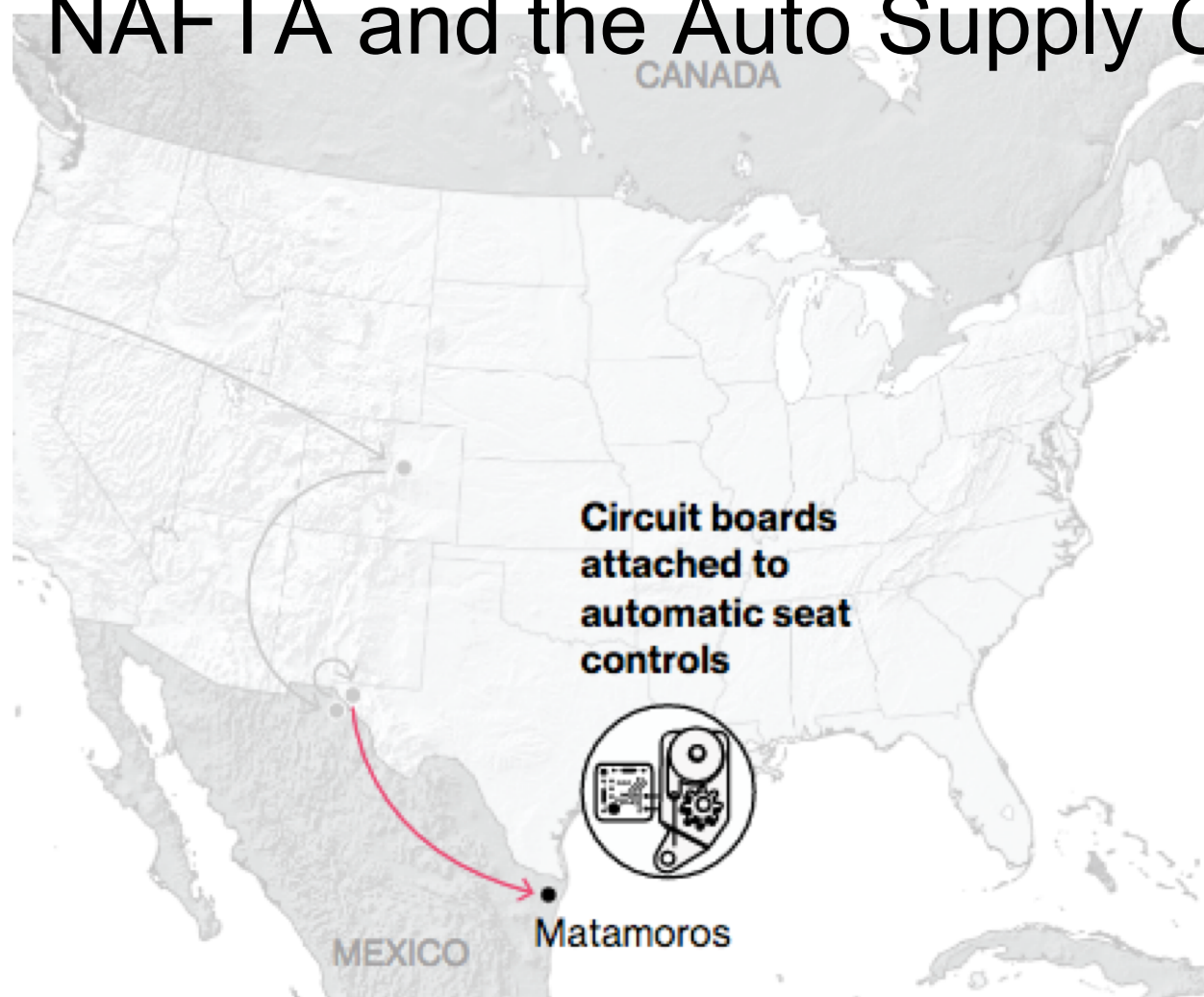
Black, Diamond, and Merrill, “One Tiny Widget’s Dizzying Journey Shows Just How Critical Nafta Has Become,” *Bloomberg*, February 2, 2017.

NAFTA and the Auto Supply Chain



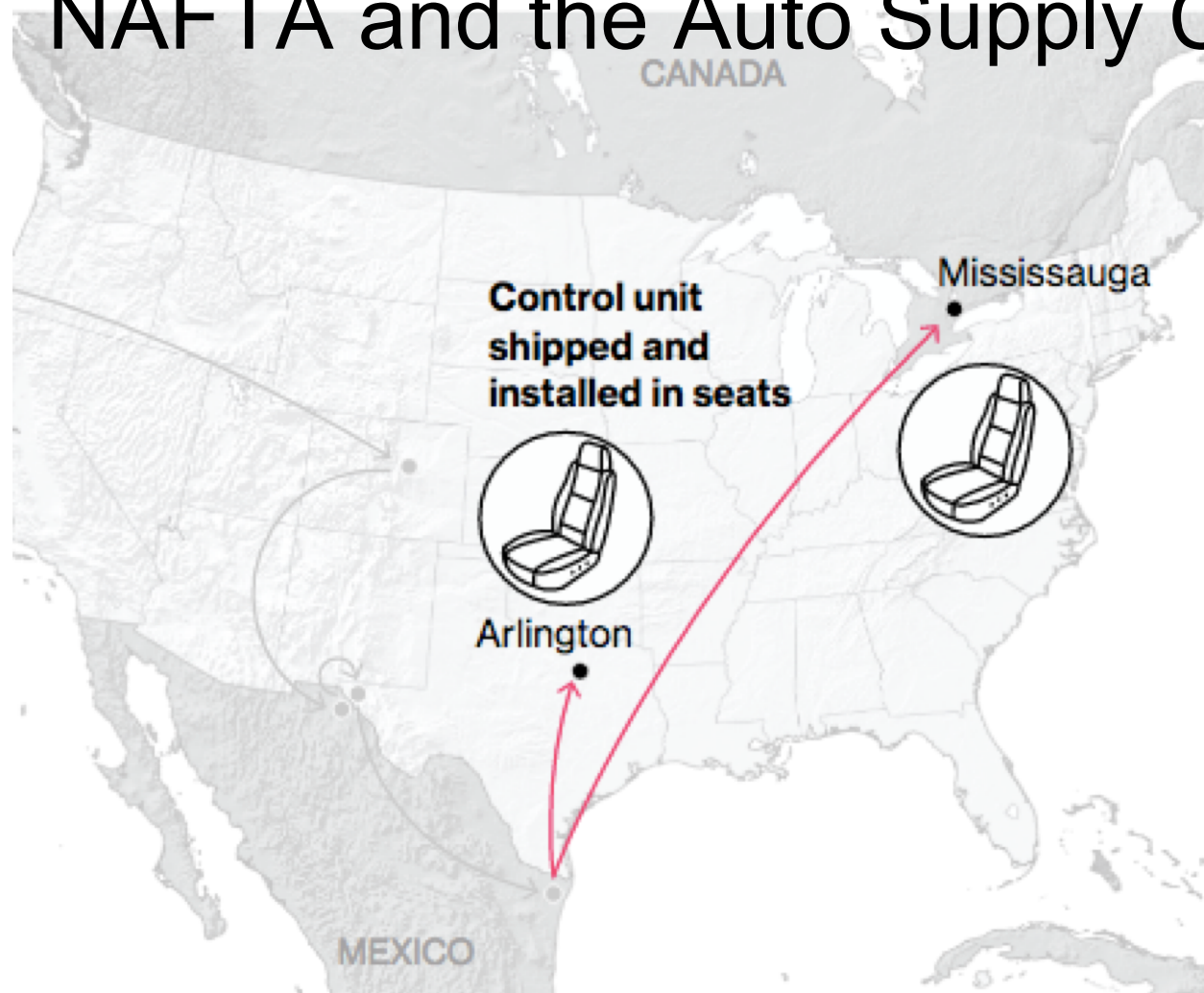
Black, Diamond, and Merrill, "One Tiny Widget's Dizzying Journey Shows Just How Critical Nafta Has Become," *Bloomberg*, February 2, 2017.

NAFTA and the Auto Supply Chain



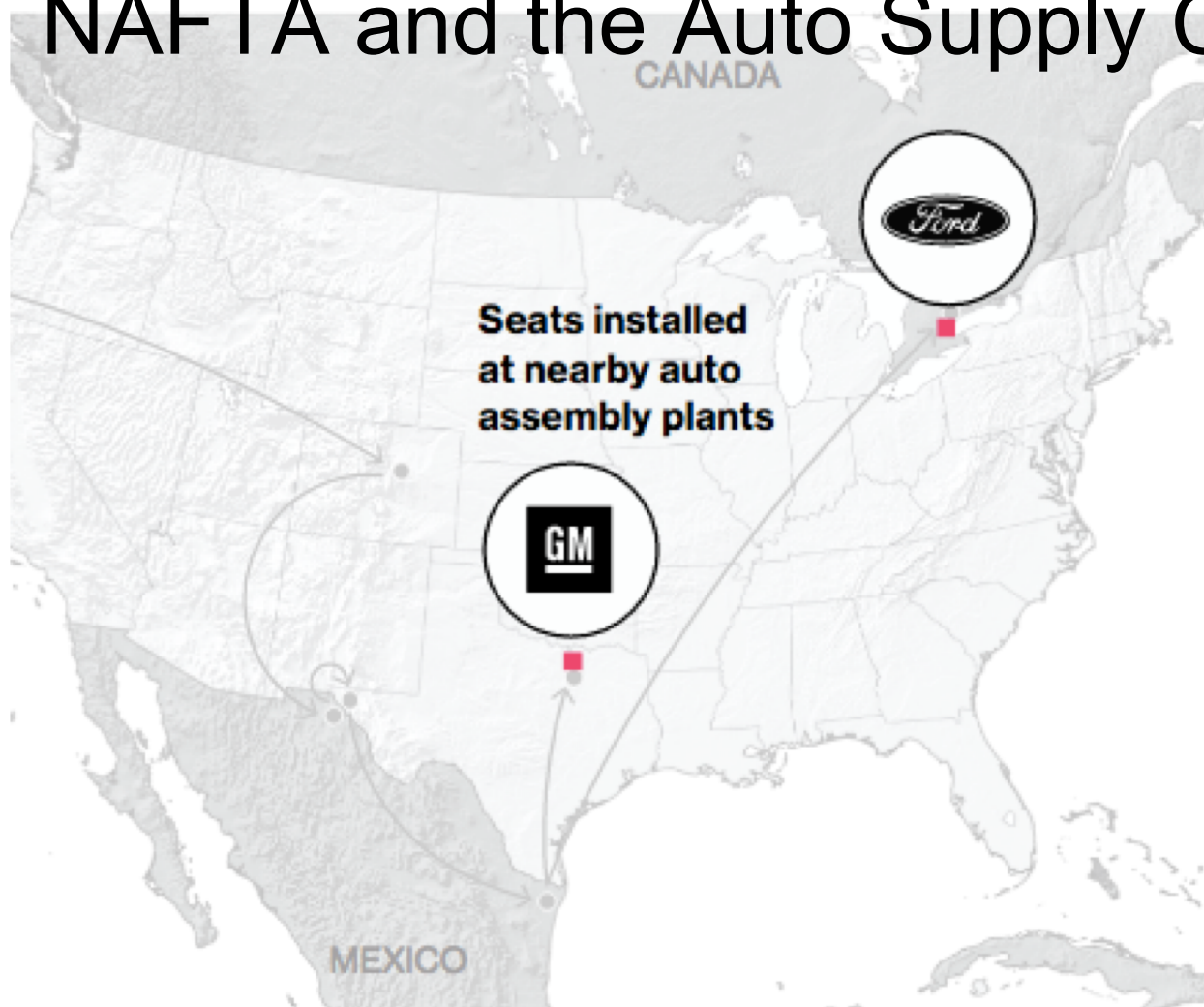
Black, Diamond, and Merrill, "One Tiny Widget's Dizzying Journey Shows Just How Critical Nafta Has Become," *Bloomberg*, February 2, 2017.

NAFTA and the Auto Supply Chain



Black, Diamond, and Merrill, “One Tiny Widget’s Dizzying Journey Shows Just How Critical Nafta Has Become,” *Bloomberg*, February 2, 2017.

NAFTA and the Auto Supply Chain



Black, Diamond, and Merrill, "One Tiny Widget's Dizzying Journey Shows Just How Critical Nafta Has Become," *Bloomberg*, February 2, 2017.

Lecture 1 Outline

Overview of the World Economy

- “Globalization”
- **Elements of the World Economy**
- Ways that Countries Interact
 - Trade
 - Capital Flows
 - Migration
- Policies that Affect Others
- Institutions

Overview of the World Economy

- International Economics
 - Is NOT about countries
 - It IS about interactions among countries

Overview of the World Economy

- World Economy consists of
 - Countries: a few hundred
(CIA lists about 240)
(WTO has 164 members)
 - People: over 7.5 billion
(7.504 billion 9/6/19,
compare 329 million US)
 - Land: about 15 times the US

(Aside, on getting information)

An excellent source of information about countries is the CIA World Fact Book
(Just Google “factbook”)



Overview of the World Economy

- World Economy consists of
 - GDP (2017 est., per CIA, in US\$)
 - World: Total = \$80.27 trillion
per capita = \$17,500
 - US: Total = \$19.49 trillion
per capita = \$59,800

Overview of the World Economy

- Implication
 - US is very unusual
 - Very rich
 - US has less than 5% of world population but almost 25% of world income
 - » (This changes, as measured here in official exchange rates, as the exchange rates change.)

Lecture 1 Outline

Overview of the World Economy

- “Globalization”
- Elements of the World Economy
- **Ways that Countries Interact**
 - Trade
 - Capital Flows
 - Migration
- Policies that Affect Others
- Institutions

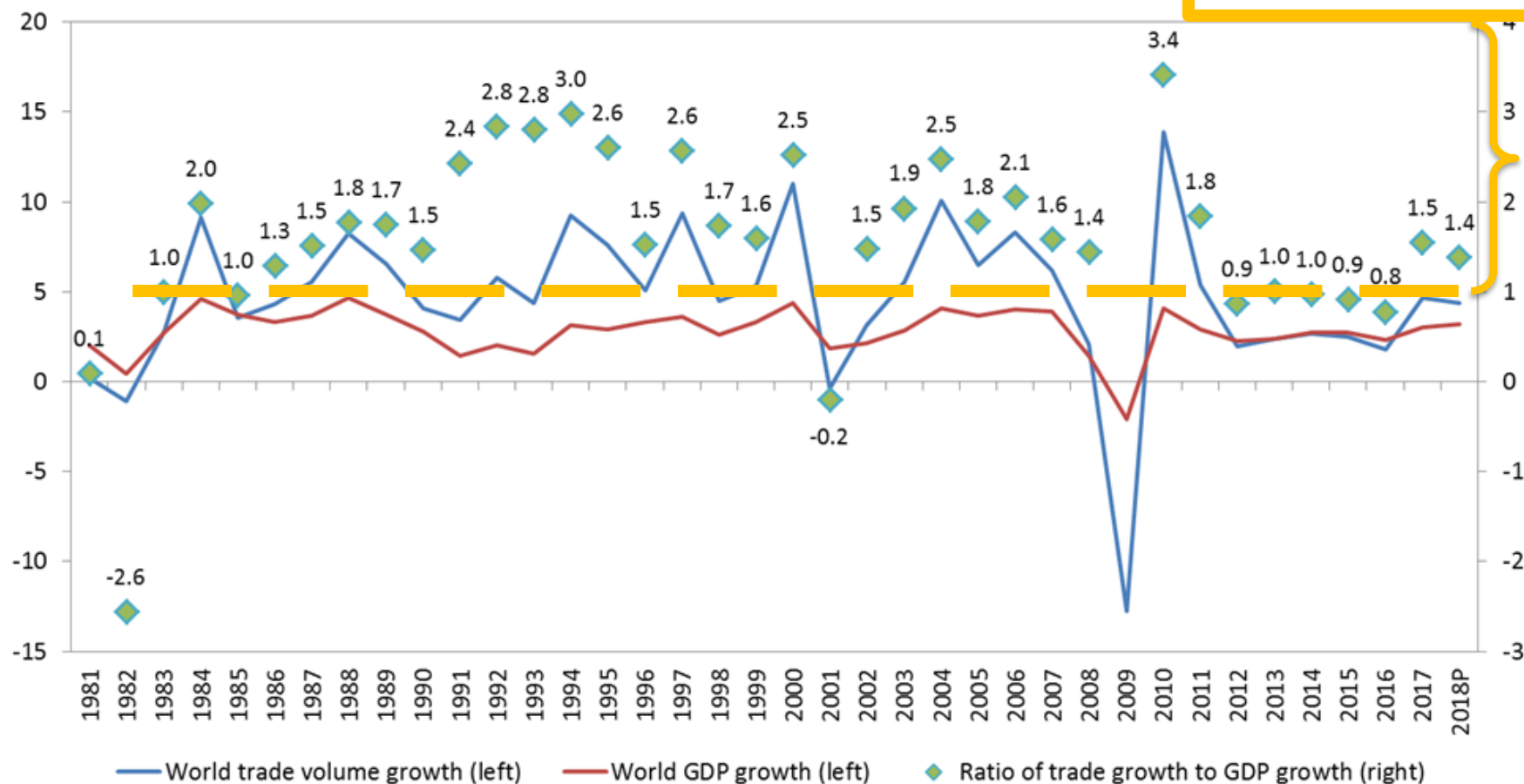
Overview of the World Economy

- Ways that countries interact economically
 - Trade (per CIA, 2017 est.)
 - World exports: \$17.31 trillion
(compare world GDP of \$80 trillion)
(That's at official exchange rates)
(Exports = 22% of GDP)
 - World trade has grown faster than world GDP most years
 - But not during 2008-9, due to world recession
 - Or during 2015-16
 - But resumed in 2017

Chart 2: Ratio of world merchandise trade volume growth to world real GDP growth, 1981-2018

% change and ratio

Trade growth
faster than GDP



Source: WTO

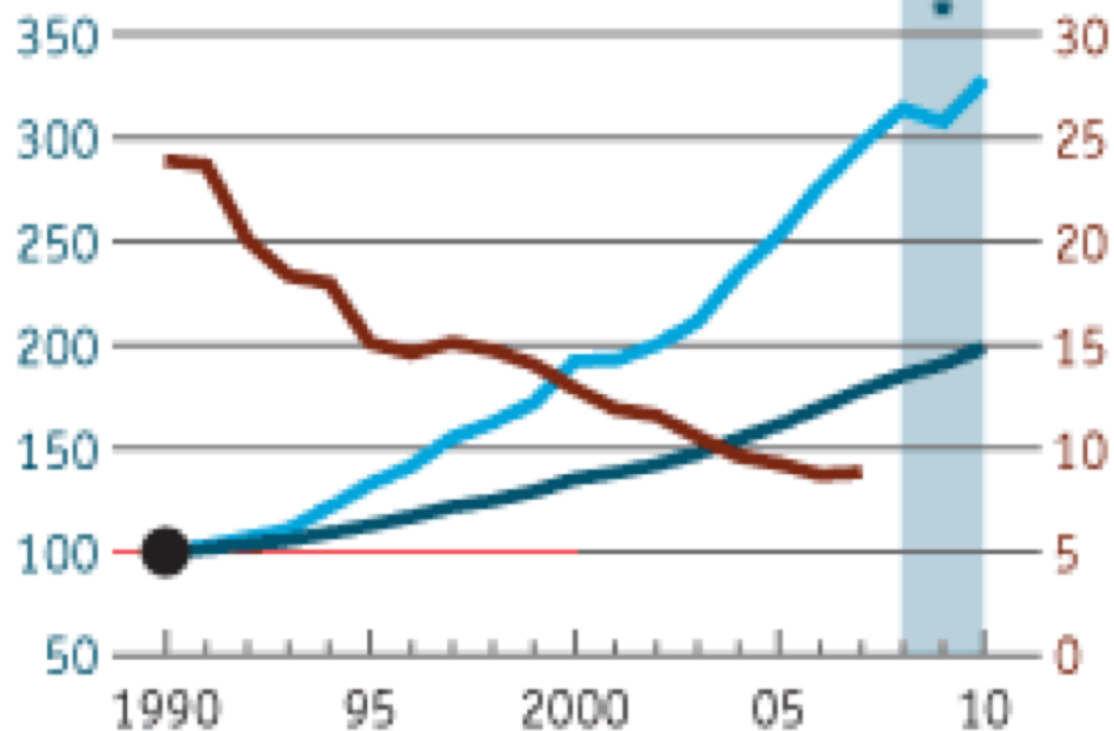
Golden years

Indices, 1990=100:

— world trade volume

— world GDP

*Average tariff
applied, %*



Sources: World Bank; IMF

*Forecast

Overview of the World Economy

- See tables below for
 - Who trades most?
 - Who trades with whom?
 - Share of trade in GDP
 - US:
 - What do we export/import?
 - To/from whom?

Who Trades the Most?

(\$ b. & % share, 2018)

Exporters			Importers		
	Value	Share		Value	Share
China	2487	12.8	US	2614	13.2
US	1664	8.5	China	2136	10.8
Germany	1561	8.0	Germany	1286	6.5
Japan	738	3.8	Japan	749	3.8
Netherlands	723	3.7	UK	674	3.4
World	19,475	100.0	World	19,867	100.0

Source: WTO, World Trade Statistical Review, 2019, Table A6

Who Trades the Most?

(Excluding intra-EU-28)

(\$ b. & % share, 2018)

Exporters			Importers		
	Value	Share		Value	Share
China	2487	16.2	US	2614	16.6
EU-28*	2309	15.1	EU-28*	2337	14.9
US	1664	10.9	China	2136	13.6
Japan	738	4.8	Japan	749	4.8
Korea, S.	605	3.9	Hng Kng	628	4.0
World	15,319	100.0	World	15,710	100.0

*EU external only

Source: WTO, World Trade Statistical Review, 2019, Table A7

Who Trades the Most?

- Developed countries are most of the biggest traders
- China has caught up, in trade volume
 - It was the #3 exporter ten years ago when I taught the course; now it's #1.
 - Others are gaining as well: Six years ago Canada was #5 exporter. Five years ago that was S Korea.

Who Trades the Most?

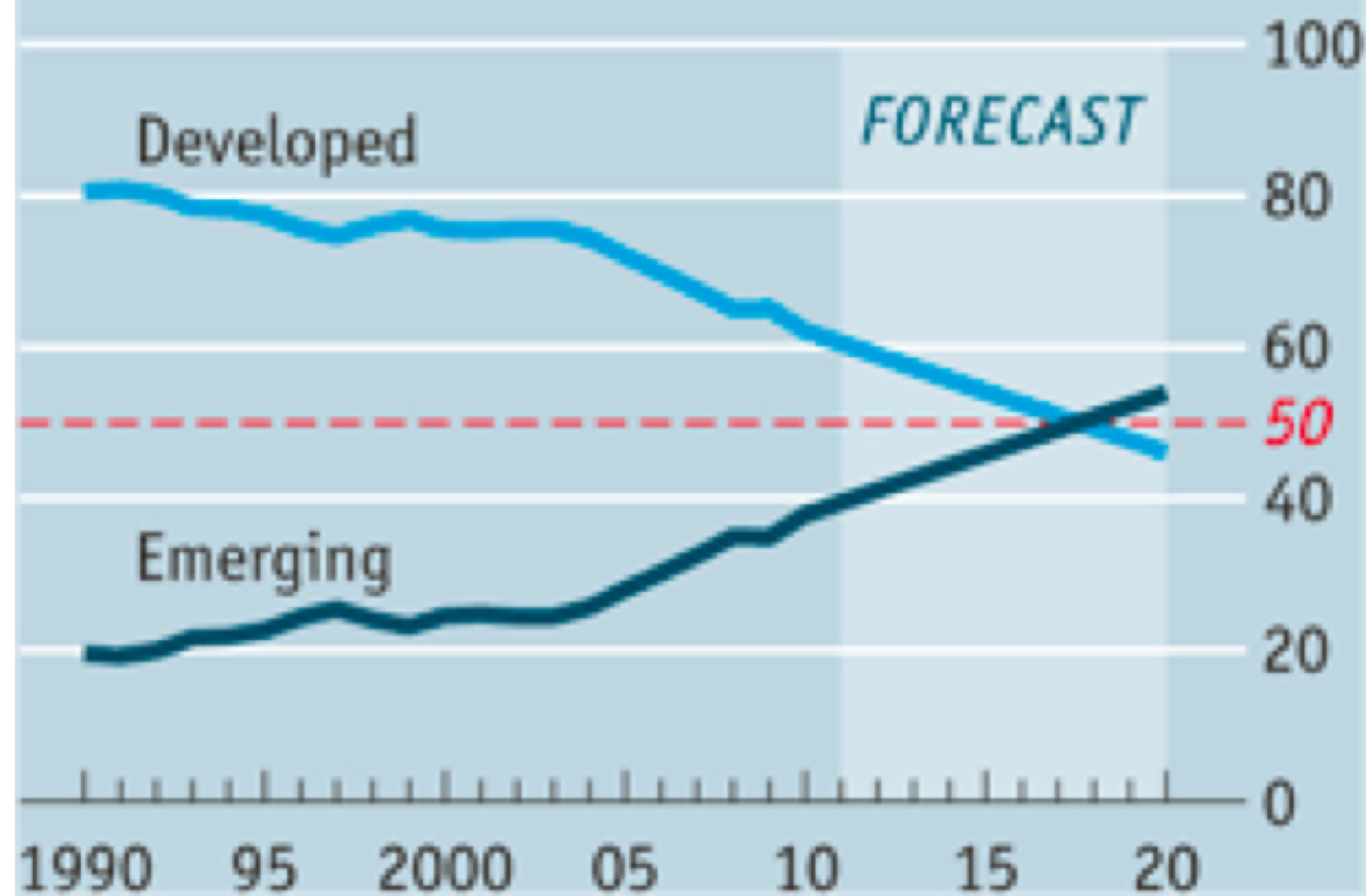
- See Economist from five years ago:
“Trading Up: Picking the world champion of trade”
 - China claimed to have surpassed US. True only for goods, not goods + services
 - But with time China will pass US in both
 - China’s trade per GDP was much larger than the US, but below world average
 - Much of the value in China’s exports is imported inputs, thus low “value added.”

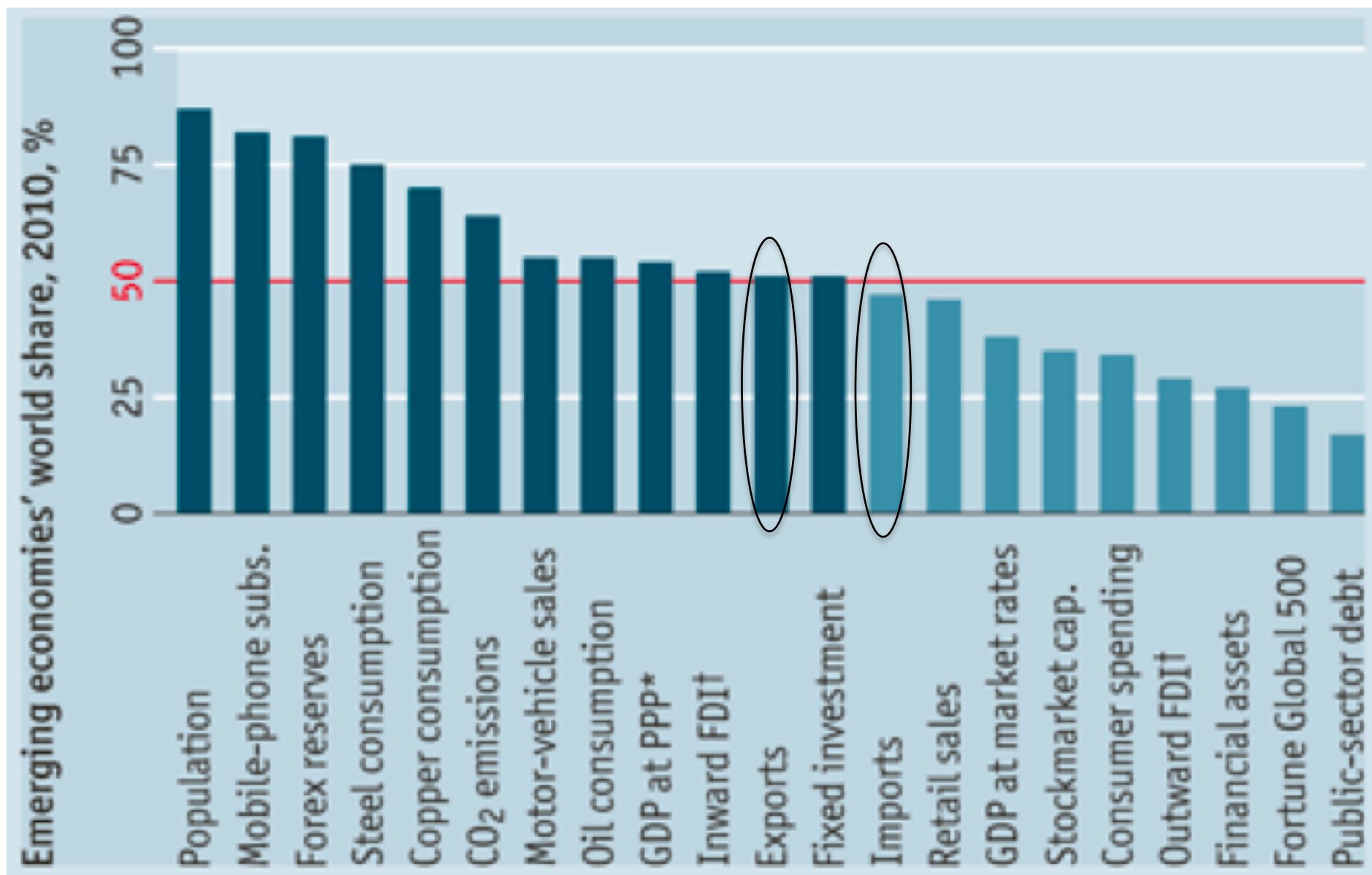
Who Trades the Most?

- “Emerging Markets” in general are catching up to, or surpassing, the developed countries
 - In GDP, trade, and more
 - See Economics Focus from *The Economist*, “Why the Tail Wags the Dog”

Economies' share of world GDP, %

At market exchange rates





Who Trades with Whom?

(\$ b., 2014, Intra- and inter-regional merchandise trade)

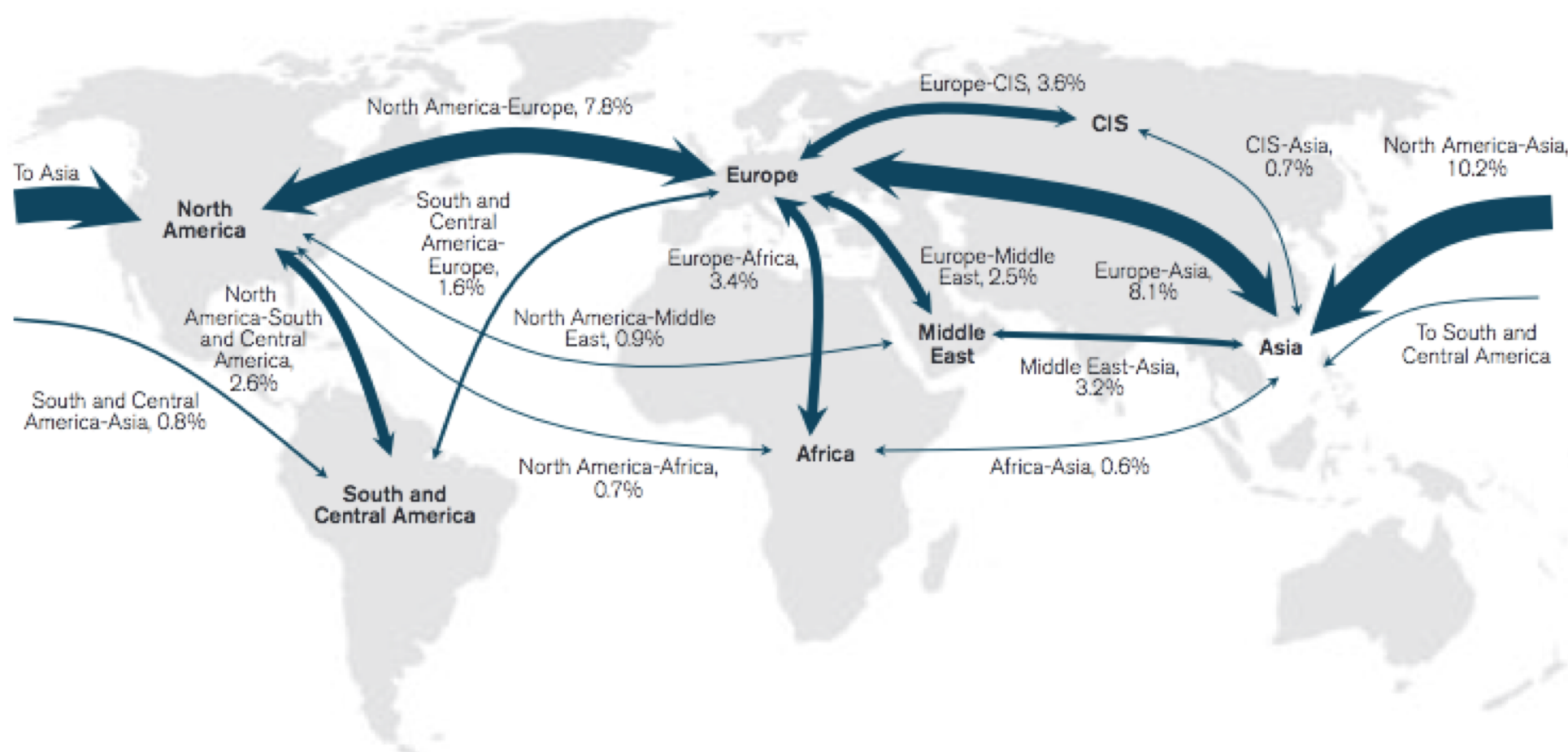
Destination:						
Origin:	North Amer.	Latin Amer.	Eur.	Asia	Africa	Other
North Amer.	1251	214	379	504	43	97
Latin Amer.	173	179	114	170	18	26
Europe	540	119	4665	738	221	447
Asia	1065	185	900	3093	207	428
Africa	39	29	201	152	98	20
Other	128	18	532	828	51	273
World	3195	744	6792	5485	639	1292

Source: WTO, International Trade Statistics, 2015, Table I.4

Note: This source is no longer published, and its replacement lacks these data.

- North America, Europe, and Asia trade mostly within their group
- Poorer regions – Latin America, Africa – trade mostly with the richer regions
- This reflects what is not so clear in the table and charts:
 - Rich countries trade most with each other
 - Poor countries trade most with rich countries
 - But their trade with each other is growing

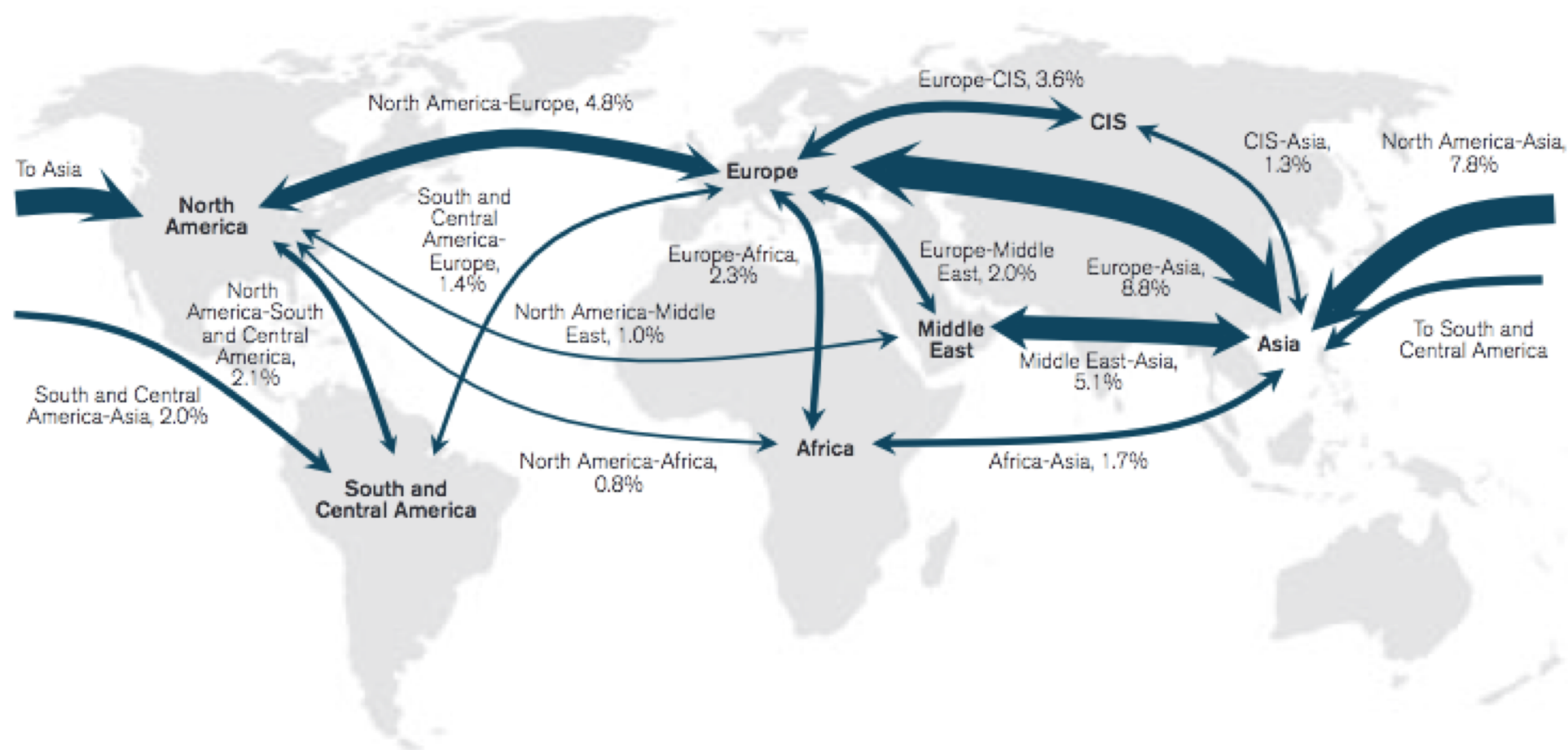
Figure B.15.A: Share of total trade between geographic regions in world trade, 1990 (percentage)



Source: WTO Secretariat estimates.

Note: World trade includes intra-EU trade. Arrow weights based on shares in 1990. Trade within regions and with unspecified destinations represented 53% of world trade in 1990.

Figure B.15.B: Share of total trade between geographic regions in world trade, 2011
(percentage)



Source: WTO Secretariat estimates.

Note: World trade includes intra-EU trade. Arrow weights based on shares in 2011. Trade within regions and with unspecified destinations represented 54% of world trade in 2011.

What Does the World Trade?

(\$ b. 2014 merchandise exports)

	Value
All Products	17,797
Agriculture	1,765
Fuels & Mining	3,789
Manuf.	12,243

Source: WTO, International Trade Statistics, 2015, Table II.1

Note: This source is no longer published, and its replacement lacks these data.

What Does the World Trade?

- Biggest traded category: manufactures
- Fastest growing, then shrinking, then growing: “fuels & mining”

Why?

- Because this is the value of trade, and prices of oil and other raw materials were rising, and then falling.

~~Did~~ (Not available since 2011) What Does the US Trade? (\$ b. 2011)

	Exports	Imports
Total	1,497.4	2,235.8
Agriculture	140.0	
Petroleum		462.3
Industrial supplies	496.4	319.8
Capital goods, exc. auto	493.2	513.4
Automotive	133.1	255.2
Other non-ag	234.6	
Other non-petrol		685.1

Source: Economic Report of the President, Feb 2013, Table B-104.

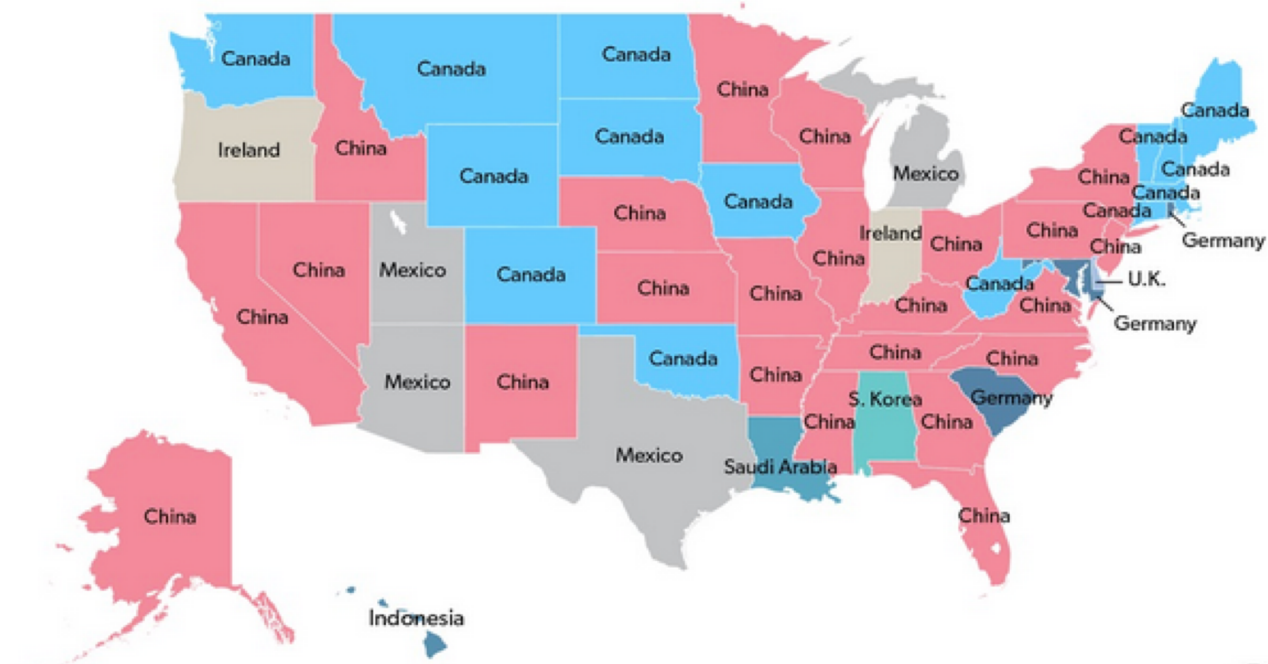
What Does the US Trade?

- US imports are much larger than US exports
 - (We'll see what that means later in the course.)
- US is a big...
 - Exporter of agricultural products
 - Importer of oil (but that's been falling)
 - Exporter and importer of capital goods (i.e., machines for making things)

Trade of US States

- US states differ substantially in the importance of international trade to them

Top Import Country for Each U.S. State (2016)

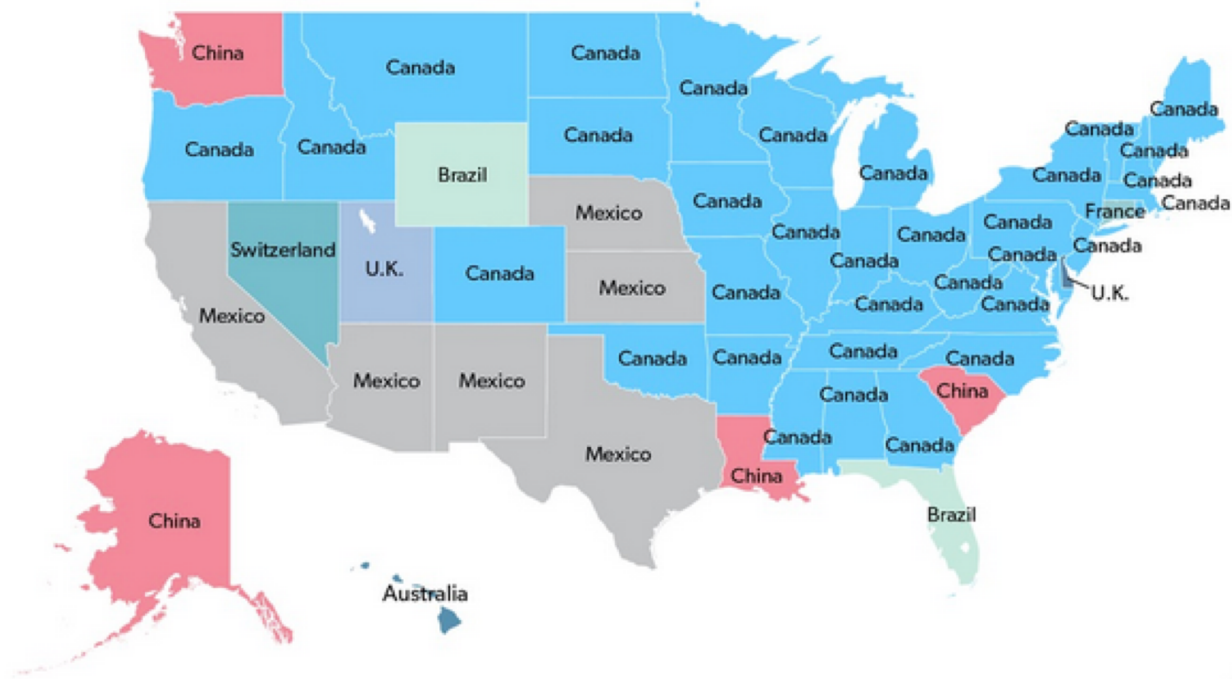


Source: US Census Bureau

Carpe Diem **AEI**

Source: Perry and Balliou (2017)

Top Export Country for Each U.S. State (2016)

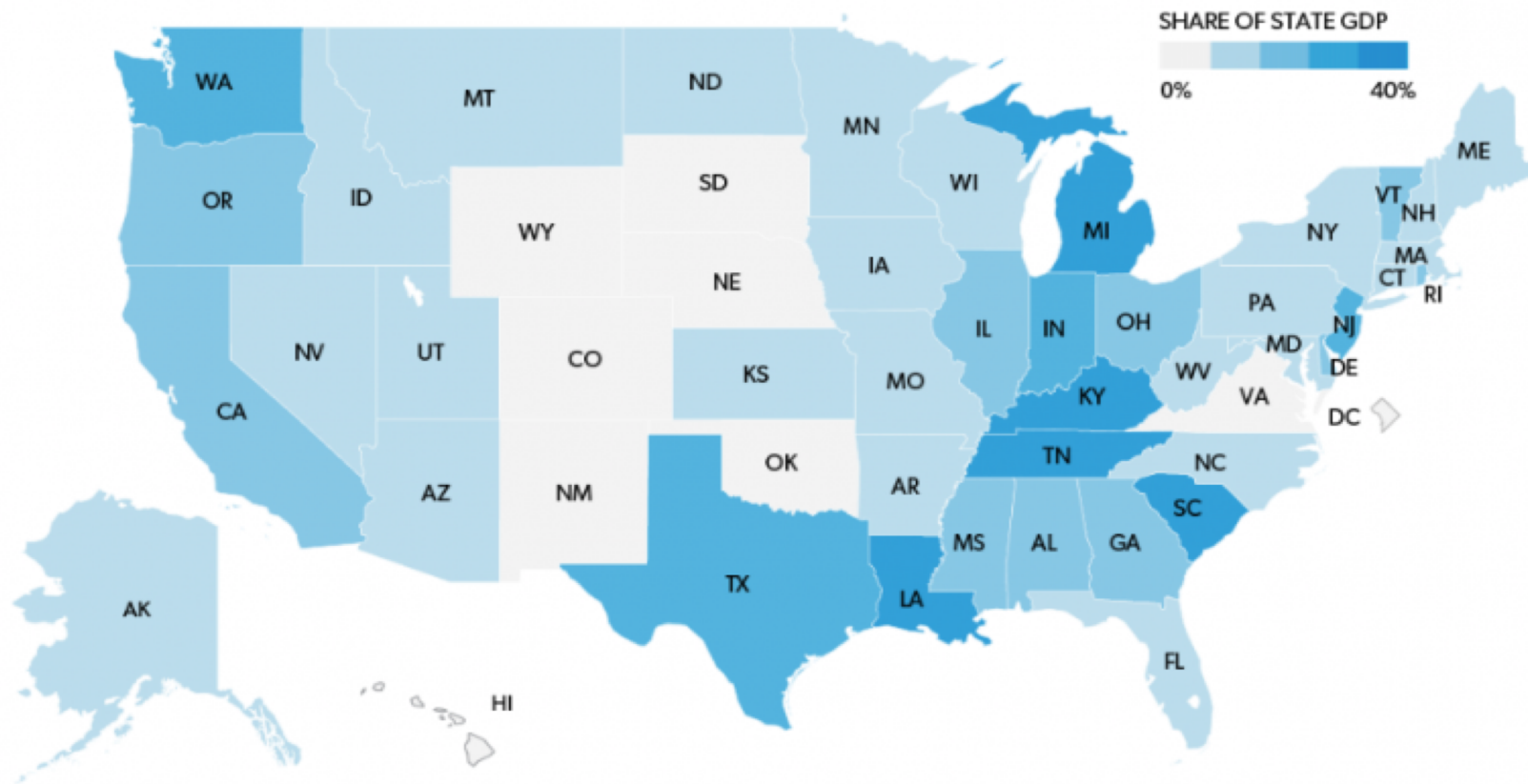


Source: US Census Bureau

Carpe Diem **AEI**

Source: Perry and Balliou (2017)

International Trade as a Share of State GDP (2016)



Source: US Census Bureau

Carpe Diem **AEI**

Source: Perry (2017)

Importance of Trade for Countries?

(GDP in US\$ b., Exports % of GDP,
Selected countries, 2017)

	Exports	Exports/GDP
United States	1553.0	8%
Japan	688.9	
Germany	1434.0	,
Canada	423.5	
India	304.1	,
Mexico	409.8	
Netherlands	555.6	,
Singapore	396.8	,
Philippines	48.2	
Nepal	0.8	,

Source: CIA World Fact Book

Importance of Trade for Countries?

- Even though we trade more than most, US trade is a smaller part of US GDP than for many other countries
- Others that are low: Japan, Nepal (even lower than US)
- Note Singapore: Exports can be more than GDP.
 - Reason: Exports are made using imported inputs, so value of exports includes imports.

Importance of Trade for Countries?

A Few More of Interest

	GDP	Exports/GDP
China	2216.0	18%
Hong Kong	537.8	
Korea, South	577.4	
Korea, North (2013)	3.0	
Burma	9.8	
Syria	1.7	
Israel	58.7	

Source: CIA World Fact Book

Lecture 1 Outline

Overview of the World Economy

- “Globalization”
- Elements of the World Economy
- **Ways that Countries Interact**
 - Trade
 - **Capital Flows**
 - Migration
- Policies that Affect Others
- Institutions

Overview of the World Economy

- Ways that countries interact economically
 - Capital Flows
 - Financial (holdings of financial assets abroad)
 - Real (international ownership of real assets)

Overview of the World Economy

- Ways that countries interact economically
 - Capital Flows
 - Financial (holdings of financial assets abroad)
 - » Currency
 - » Bank deposits
 - » Bonds – private and government
 - » Stocks
 - » Bank loans
 - Real (international ownership of real assets)

Overview of the World Economy

- Ways that countries interact economically
 - Capital Flows
 - Financial (holdings of financial assets abroad)
 - Real (international ownership of real assets)
 - » Real estate
 - » Capital assets (plant and equipment)
 - » Stocks (equities) if ownership share is large
 - » Other

Data, below, are stocks (i.e, amounts at a point in time)

US Investment Position

(\$ trillion at market value, end of 2018)

	We “Own” US Assets	We “Owe” US Liabilities
Total*	25.24	34.80
Direct investment	7.50	8.48
Portfolio investment	11.49	18.72
Other investment	4.30	6.14
Reserve assets	0.45	

Compare: US GDP in 2017 = \$19.39 trillion

*Excludes financial derivatives other than reserves. Would add net +0.06.

Source: Bureau of Economic Analysis, U.S. Net International Investment Position

US Investment Position

- (Qualification: “Owe” may not be quite right. This may include all assets in the US owned by foreigners, including land, buildings, etc. Not just what we’ve borrowed.)
- Lessons:
 - US is a large net “debtor” (result of our spending more than we earn)

Lecture 1 Outline

Overview of the World Economy

- “Globalization”
- Elements of the World Economy
- **Ways that Countries Interact**
 - Trade
 - Capital Flows
 - **Migration**
- Policies that Affect Others
- Institutions

Overview of the World Economy

- Other ways that countries interact economically
 - Migration
 - Temporary
 - Guest workers
 - Day workers
 - Permanent
 - In practice, most (all?) countries limit migration severely

Clicker Question

Which category of goods is largest in world trade

- ✓ a) Manufacturers
- b) Fuels and mining
- c) Agriculture

Clicker Question

Which is the world's largest importer?

- a) China
- b) European Union
- ✓ c) US
- d) Germany

Clicker Question

Where does the largest share of Michigan's imports come from?

- a) Canada
- b) China
- ✓ c) Mexico
- d) European Union

Lecture 1 Outline

Overview of the World Economy

- “Globalization”
- Elements of the World Economy
- Ways that Countries Interact
 - Trade
 - Capital Flows
 - Migration
- **Policies that Affect Others**
- Institutions

Overview of the World Economy

- Other ways that countries interact economically
 - Policies that affect other countries
 - Direct
 - Indirect

Overview of the World Economy

- Other ways that countries interact economically
 - Policies that affect other countries
 - Direct
 - Trade policies (tariffs, quotas)
 - Foreign aid
 - Capital controls
 - Exchange rate management
 - Immigration restrictions
 - Indirect

Overview of the World Economy

- Aside on Tariffs
 - We will be dealing a lot with these
 - US tariffs are much lower than they used to be (average less than 4% now, vs. 40% in 1946)
 - (Tariffs have gone up under Trump, but average is still low.)
 - US has gained a great deal from lowering tariffs
 - US still has much to gain from further lowering
 - But there are also severe costs for some people and firms who compete with imports

Overview of the World Economy

- Aside on Tariffs
 - Tariffs could go up, even legally:
 - WTO enforces only upper limits on tariffs
 - Actual tariffs in many countries are below these limits, and could legally rise
 - There was danger that the world recession of 2008 would push countries to do that.
 - They didn't – at least not much.
 - Some tariffs have gone up this year under Trump
 - We'll see more next time

Overview of the World Economy

- Aside on Tariffs
 - US tariffs are much higher against developing countries than against developed countries

Overview of the World Economy

- Aside on Tariffs
 - Until recently, much trade policy has been Trade Agreements, by countries that reduce tariffs.
 - This trend has now stalled for the US under President Trump,
 - though he is trying for “deals” with EU and Japan.
 - But other countries are continuing it without Trump.

Overview of the World Economy

- Other ways that countries interact economically
 - Policies that affect other countries
 - Indirect
 - Subsidies (esp. agriculture)
 - » US farm subsidies > foreign aid
 - » Macro policies (monetary, fiscal)
 - Environmental policies
 - Standards
 - » Labor
 - » Health & safety
 - » Norms

Lecture 1 Outline

Overview of the World Economy

- “Globalization”
- Elements of the World Economy
- Ways that Countries Interact
 - Trade
 - Capital Flows
 - Migration
- Policies that Affect Others
- **Institutions**

The Three Main Institutions

- Functions
 - IMF (International Monetary Fund): Financial Assistance
 - World Bank: Development Assistance
 - WTO (World Trade Organization): Trade Policy Regulation and Negotiation

The Three Main Institutions

- History

- Before World War II

- Great Depression
 - High Tariffs on trade
 - Competitive Devaluations of Currencies

“Beggar Thy Neighbor Policies”
(we’ll see why later)

The Three Main Institutions

- History
 - End of World War II
 - Bretton Woods Meeting (Bretton Woods, NH)
 - IMF
 - World Bank
 - GATT (General Agreement on Tariffs and Trade)
 - » Succeeded by WTO in 1995

The Three Main Institutions

- History: Changes since 1940s
 - IMF
 - Originally enforced pegged exchange rates
 - IMF now provides financial assistance
 - » E.g., Argentina just asked IMF for help
 - World Bank (=IBRD, International Bank for Reconstruction and Development)
 - Originally intended for reconstruction from war
 - Now mainly assists development
 - GATT/WTO
 - Rules of international trade policy
 - Ministerial Meetings

Clicker Question

Compared to the 1940s, US tariffs today (as of 2017) are?

- a) Higher
- b) About the same, on average
- c) Half as large
- ✓ d) Only about 1/10 as large
- e) Gone

Clicker Question

Which institution also goes by the acronym IBRD?

- a) International Monetary Fund
- ✓ b) World Bank
- c) World Trade Organization

IBRD = International Bank for Reconstruction and Development

Next Time

- Current Tensions in the International Economy
 - NAFTA
 - Brexit
 - Trade War
 - WTO
 - Currencies