International Trade: Theory and Politics
Lecture 1 - Introduction
Miroslav Zajíček
University of Economics in Prague
Technical data

• Primary instructor: Dr. Miroslav Zajicek, NB 349
• E-mail: miroslav.zajicek(at)vse.cz
• Exam: Final (only), all past exams of the Course Materials webpage (go through kie.vse.cz)
• Hours for Students: Tuesdays 14:30 – 16:30
• Sylabus: available at kie.vse.cz Course Materials (detailed) or in the ISIS (general)
Sky disk of Nebra

• Produced some time in 16th century BC
• Founded in Germany, south of Berlin as a part of a treasure
• Material was mined in todays Austria
• A long distance trade was here very loooong ago
Case study I: „Impact of the naval disaster“

• 1688 Glorious revolution
• 1690 Beachy Head defeat
• 1693 Smyrna expedition disaster
• 1694 Creation of the Bank of England to finance new Royal Navy
Case study II: Two waves of globalization (1)

Figure 1.9 Foreign capital stocks; assets/world GDP

Source: Based on Obstfeld and Taylor (2003).
Case study III: International financing of the Louisiana Purchase and its irony

- December 20, 1803
- By far the BEST real estate deal in history (second best deal was Alaska purchase from Russia in 1867 for 7.2 mil. USD)
- USA primarily interested in New Orleans
- Purchasing price – 15 mil. USD for 828,000 sq. miles
- Financed by Hope & Co. in Amsterdam and Barings & Co. in London by bond issue (IR = 6%) – both still exist
- Russia bought most of the bonds! (i.e. Napoleon financed his war against Russia by its own money)
- 1804 – Lewis and Clarke expedition embarked on charting new territory
- There are other similar deals in the US history (see below the list)
Louisiana Purchase – the map
Case study III: Other „US Real Estate“ Deals in History (part 1)

<table>
<thead>
<tr>
<th>Date</th>
<th>Treaty or Act</th>
<th>Property</th>
<th>From</th>
<th>Total Area (thousand acres)</th>
<th>Price (thousand USD)</th>
<th>Price per Accre (cents)</th>
</tr>
</thead>
<tbody>
<tr>
<td>1803</td>
<td>Louisiana Purchase</td>
<td>Louisiana</td>
<td>France</td>
<td>559,514</td>
<td>15,000</td>
<td>3</td>
</tr>
<tr>
<td>1819</td>
<td>Adam-Onís Treaty</td>
<td>East Florida</td>
<td>Spain</td>
<td>46,145</td>
<td>15,000</td>
<td>33</td>
</tr>
<tr>
<td>1846</td>
<td>Oregon Treaty</td>
<td>Pacific Northwest south of 49th parallel</td>
<td>Great Britain</td>
<td>192,000</td>
<td>-</td>
<td>0</td>
</tr>
<tr>
<td>1848</td>
<td>Guadalupe-Hidalgo</td>
<td>Texas, California, New Mexico</td>
<td>Mexico</td>
<td>338,681</td>
<td>15,000 +5,000</td>
<td>6</td>
</tr>
</tbody>
</table>
### Case study III: Other „US Real Estate“ Deals in History (part 2)

<table>
<thead>
<tr>
<th>Date</th>
<th>Treaty or Act</th>
<th>Property Description</th>
<th>From</th>
<th>Total Area (thousand acres)</th>
<th>Price (thousand USD)</th>
<th>Price per Accre (cents)</th>
</tr>
</thead>
<tbody>
<tr>
<td>1850</td>
<td>Texas Cession</td>
<td>New Mexico</td>
<td>Texas</td>
<td>78,927</td>
<td>10,000</td>
<td>13</td>
</tr>
<tr>
<td>1853</td>
<td>Gadsden Purchase</td>
<td>Southern Arizona, New Mexican border</td>
<td>Mexico</td>
<td>18,989</td>
<td>10,000</td>
<td>53</td>
</tr>
<tr>
<td>1867</td>
<td>Alaska Purchase</td>
<td>Alaska</td>
<td>Russia</td>
<td>375,296</td>
<td>7,200</td>
<td>2</td>
</tr>
<tr>
<td>1898</td>
<td>Treaty of Paris</td>
<td>Philippines</td>
<td>Spain</td>
<td>74,112</td>
<td>20,000</td>
<td>27</td>
</tr>
</tbody>
</table>
Case study IV: Ming Trade (1)

• During the Song (960-1279) and early Yuan (1279-1320), China's foreign trade expanded
• Mid-1270s to late 1400s, several economic and monetary contractions: „the economic depression of the renaissance"
• Ming dynasty (1368-1644) making recoveries by 1492:
  – Population 100 million
  – European, Middle Eastern and Asian markets bought raw silk, silk textiles, and porcelains
Case study IV: Ming Trade (2)

• Pre-Columbus, the Ming were facing monetary problems
  – Late Yuan (1279-1368) notes were not backed with metals; failed to hold value
  – Ming currencies were no more successful. Copper coins were the dominant currency
  – Silver was valuable by world standards

• Silver from the new world began to enter China through three routes:
  – 1) From Acapulco to Manila, the Spanish capital of the Philippines from 1571
  – 2) „Treasure fleets“ that brought gold and silver back to Spain and Portugal, where it entered general circulation. Portuguese trade was centered on Macao
  – 3) Via the Dutch and English East India Companies, who bought pepper, spices, cottons, silks and porcelains

• Japanese silver mining and Sino-Japanese trade also expanded during the late Ming
Case study IV: Ming Trade (3)

• Impacts on the Ming economy:
  – Sharp rises in receipts of silver by central and local governments. Implementation of the „Single Whip Method" of taxation
  – Widening of the gold-silver ratio, mirroring the rest of the world
  – Increased agricultural specialization and commercialization, growth in the silk, cotton, and porcelain industries, especially in the lower Yangtze
  – Greater vulnerability (especially of the money supply) to foreign events
  – By the 1640s, cheap copper coins and declining silver imports began to drive silver out of the market in the southeast
Case study V: Qing Trade (1)

• Qing dynasty (1644-1912)
• 1640s and 50s were a time of widespread poverty, unemployment, deflation, unsold inventories, and scarce money. Population declined
• 1661, government orders people along the coast to move 17 miles inland; few people engaged in foreign or coastal trade
• Things begin to turn around in 1700: population and life expectancy rise, markets became more integrated
Case study V: Qing Trade (2)

• Foreign trade was centered on Canton and Macao (silk, ceramics, sugar, sandals exported in return for silver and pepper)
• Canton trade with Europe grew 4% a year from 1719 to 1806
• But the trade was (according to some views) tightly controlled: from 1704 designated merchants delivered revenue to the throne for the right to trade with foreigners
• From 1760 to the Opium War, the „Canton system" subordinated foreign merchants to the Cohong (licensed monopolists), and the Cohong to the Hoppo (superintendent of customs)
Case study V: Qing Trade (3)

FIGURE 1.—GROWTH OF THE TREATY PORT SYSTEM

Legend
- wave1 Events
- wave2 Events
- wave3 Events
- wave4 Events

Source: Jia (forthcoming) RESTAT
Case study V: Qing Trade (4)

**Figure 2B.** Trends of population size from 1776 to 2000 combining waves (population in 10,000)

Source: Jia (forthcoming) RESTAT
Impact of international capital flows

• Both countries are better off DESPITE the fact that in one country interest rate rose
Feldstein – Horioka puzzle

• Based on empirical study of Feldstein – Horioka (1980)
• Correlation between S and I very high – close to one (as opposed to the theory)
• Implication: international capital market integration and international capital mobility is STILL RATHER LIMITED (as opposed to popular view of highly globalized financial markets)
• However, data after 1980 indicate increasing market integration and decreasing correlation of S and I
Three trade regimes, three trade theory families

• Regime 1: The Industrial Revolution
  – New technologies drive the increase in production
  – Ricardian theory (comparative advantage) explains technology-driven trade growth

• Regime 2: The late nineteenth century
  – Falling transportation costs drive trade growth
  – Heckscher-Ohlin (neoclassical) theory may better explain trade

• Regime 3: The twentieth century
  – Product differentiation becomes more important
  – Multilateral trading networks dominate
  – New Trade Theory (Krugman et al.) is a likely explanation
Adam Smith (1723 – 1790)

• Scottish philosopher, considered as a founder of modern economics
• Author of the *Theory of Moral Sentiments* (1756) and *An Inquiry into the Nature and Causes of the Wealth of Nations* (1776)
• Famous for „invisible hand theorem“ – people pursuing their own self-interest benefit society as a whole
• Advantages of increasing specialization / division of labour (the pin factory example and the division-of-labour-is-limited-by-the-extent-of-the-markets)
Comparative advantage – Smithian contribution

• Opportunity costs in regulation in general

“no regulation of commerce can increase the quantity of industry in any society beyond what its capital can maintain“

• Application of opportunity cost principle to individuals in society

“it is a maxim of every prudent master of the family, never ti attempt to make at home what it will cost him more to make than to buy“