International Trade and the Multinational Firm

Time / Location: Thursday, 12 - 14, HS 414

Outline: The lecture starts out with theories of international trade based on comparative advantage (Ricardo and Heckscher-Ohlin) followed by theories based on monopolistic and oligopolistic competition to explain intra-industry trade. The final part covers firm heterogeneity and multinational firms. [If time permits the Armington model and the standard neoclassical model will be addressed.]

Lecture slides are provided via WueCampus.

The lecture is accompanied by a tutorial (Übung) which gives you the opportunity to practice the material covered. Problem sets are provided via WueCampus. You are expected to work out the problems before the tutorials take place.
Textbooks


A detailed list of references with further references, notably journal articles, is provided with each chapter of the lecture
Structure of the Lecture

I  Ricardian Trade Theory

II  Heckscher-Ohlin Trade Theory

III  New Trade Theory: Intra-Industry Trade, Increasing Returns to Scale, Imperfect Competition

IV  Firm Heterogeneity, Trade and FDI

V  The Multinational Firm

If time permits we may also address the following topics:

VI  Armington Model and an Introduction to Trade Theory with Numbers

VII  The general neoclassical model – closed economy

VIII  The general neoclassical model of international trade

IX  Sector-specific factors: The Ricardo-Viner model
The Composition of World Trade


World Merchandise Trade – Regional Shares


- the 'triad' (North-America, Europe/Asia) dominates world trade
- a large amount of trade takes place within these blocs
The Changing Nature of World Trade

Once upon a time, comparative advantage looked pretty good as a description of trade ...

Composition of British trade circa 1910

Source: Krugman (2008) – Nobel Lecture Slides
... but over time it got hard to see much difference between what countries exported and what they imported

Source: Krugman (2008) – Nobel Lecture Slides
Furthermore, trade increasingly seemed to be between similar countries.

Source: Krugman (2008) – Nobel Lecture Slides
More broadly, rise of intraindustry trade

Source: Krugman (2008) – Nobel Lecture Slides

Note: The Grubel-Lloyd index is the fraction of total trade that is accounted for by intraindustry trade.
Trade Theories: An Overview provided by the WTO

Table 7
Trade theories

<table>
<thead>
<tr>
<th></th>
<th>Traditional trade theory</th>
<th>“New” trade theory</th>
<th>Heterogeneous firms models</th>
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</thead>
<tbody>
<tr>
<td>Gains from trade (causes)</td>
<td></td>
<td></td>
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<tr>
<td>Specialization</td>
<td>Yes</td>
<td>No</td>
<td>No</td>
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<tr>
<td>Economies of scale</td>
<td>No</td>
<td>Yes</td>
<td>Yes</td>
</tr>
<tr>
<td>Pro-competitive</td>
<td>No</td>
<td>Yes</td>
<td>No</td>
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<tr>
<td>Variety</td>
<td>No</td>
<td>Yes</td>
<td>No¹</td>
</tr>
<tr>
<td>Aggregate productivity (through selection/reallocation)</td>
<td>No</td>
<td>No²</td>
<td>Yes</td>
</tr>
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<td>Trade patterns</td>
<td></td>
<td></td>
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<tr>
<td>Inter-industry</td>
<td>Yes</td>
<td>No</td>
<td>No</td>
</tr>
<tr>
<td>Intra-industry</td>
<td>No</td>
<td>Yes</td>
<td>Yes</td>
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<tr>
<td>Exporters and non-exporters within industries</td>
<td>No</td>
<td>No</td>
<td>Yes</td>
</tr>
<tr>
<td>Distribution</td>
<td></td>
<td></td>
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<td>Trade liberalization affects relative factor rewards</td>
<td>Yes</td>
<td>No</td>
<td>No</td>
</tr>
</tbody>
</table>

¹ Variety effects are ambiguous. See Section C.3.

² In the Krugman model, “productivity” in the integrated market also increases in the sense that the same total amount is produced at lower average cost due to exploitation of scale economies. However, the Krugman model is silent about which firms remain in business, since it does not include differences among firms. Once firms are distinguished according to their productivity level, as in the Melitz model, the exit of less productive firms itself leads to improvements in overall industry productivity.

Note: The table refers to the basic versions of the models (row 2). As discussed in the text, models that combine features from different approaches presented in the table have been developed.

Source: Based on Table 1 of Bernard et al. (2007a).