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## Economics & Society



## Lecture 11 Labor Market & Trade

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## Previously in E&S...

- ★ The commodity market   
households, firms, the government, foreign sector
- ★ Equilibrium in the commodity market   
when  $Y = C + I + G$
- ★ Links between the markets:
  - ▶ Output  $\rightarrow$  money demand  $\rightarrow$  interest rate
  - ▶ Interest rate  $\rightarrow$  investment  $\rightarrow$  output.
- ★ Fiscal policy through  $G$  vs.  $t$
- ★ Monetary policy and stabilization
- ★ Crisis\_

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## Labor Market – Trade

Estimated duration: 100min



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### Local vs. Global

- Cultural
- Historical
- Geographical
- Political
- Economical

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World trade
> International trade

- ★ Once uncommon, foreign products are now **everywhere**  
from toothpicks to electric cars
- ★ Nowadays, it is **not easy** to even tell **where** a product was really made
- ★ Take, **for instance**, the most iconic US product, the **iPhone**:
  - ▶ **Designed** in California
  - ▶ **Assembled** in China
  - ▶ From **parts** produced in Korea, Germany, Japan, and the US
  - ▶ From **resources** extracted in Russia, South Africa etc.
- ★ **Services** follow a similar pattern of **outsourcing**:
  - ▶ **Customer** support
  - ▶ **Services** that can be communicated electronically

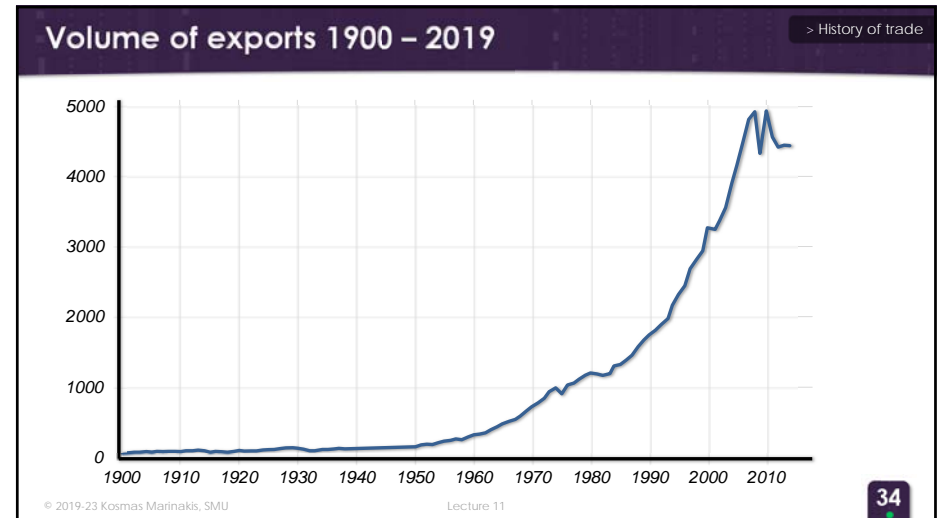
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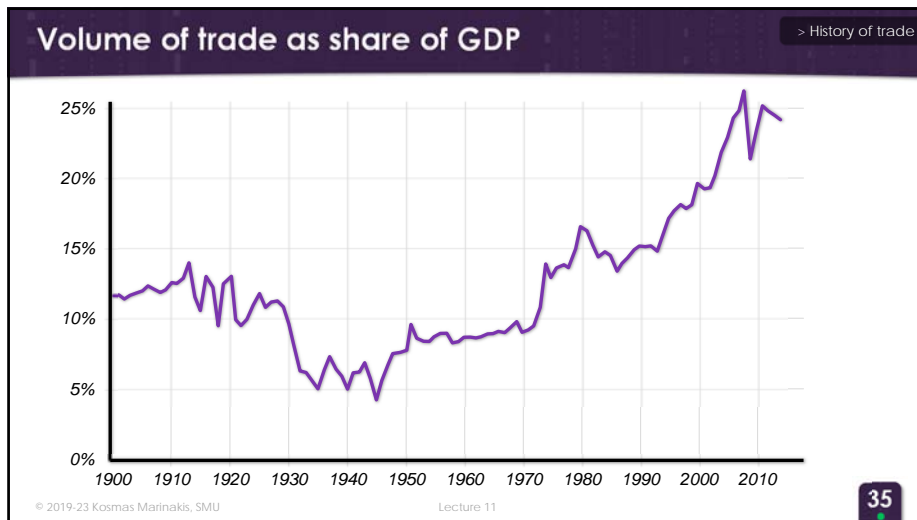
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### 1900 – 1959

> History of trade

- ★ It became possible to have global trade after having in place several **basic technologies**
- ★ The **beginnings** of the global economy was in fact more than a century ago people in **England** were able to buy **Chinese tea** in the 1910s
- ★ Between the two World Wars international commerce was **reduced** as a share of the GDP:
  - ▶ Not so much because of the **war**
  - ▶ Because of **restrictions** such as tariffs and quotas.
- ★ **By 1960** trade as a share of GDP was **below** the level of **1910**.

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### 1960 – today

> History of trade

- ★ There has been an **increase** in the volume of world commerce from 1960
- ★ Supported by new **technological breakthroughs**
- ★ Till the 1980s the increase has been **moderate** relative to the size of the economy
- ★ International commerce **increased rapidly** from the 1990s this period sometimes is referred to as “**hyper-globalization**”
- ★ There is some evidence that nowadays international trade has **leveled off**.

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## The economic driving force

> The economics of trade

- ★ Trade allows for **division of labor** and **specialization**
- ★ Those make the world **richer** in **2 ways**:
  1. Allow nations to **concentrate** on what they do better:
    - ▶ Greece has a superior **hospitality** industry than Singapore
    - ▶ Singapore has better **trade** services than the US.
  2. Allow for the development of **economies of scale**  
producing fewer things at much higher quantities leads to **cost reduction**.

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## Absolute advantage

> The economics of trade

- ★ In 1817, the British economist **David Ricardo** offered the first example for the benefits from trade:
  - ▶ England
  - ▶ Portugal
- ★ A country has the **absolute advantage** in the production of a good when it can produce it **using fewer resources**.

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## Comparative advantage

> The economics of trade

- ★ What if a country is **better** in the production of **both** goods?:
  - ▶ Singapore can produce either **100 units of banking** OR **50 units of tourism** per year
  - ▶ Cyprus can produce either **50 units of banking** OR **40 units of tourism** per year.
- ★ **1 unit of tourism costs:**
  - ▶ **2 units of banking** to Singapore
  - ▶ **1.25 units of banking** to Cyprus.
- ★ **1 unit of banking costs:**
  - ▶ **0.5 units of tourism** to Singapore
  - ▶ **0.8 units of tourism** to Cyprus.
- ★ Singapore should focus on **banking**, Cyprus on **tourism**, and **trade**
- ★ Singapore has the **comparative advantage** in **banking** and Cyprus in **tourism**  
a country has the **comparative advantage** in what it can produce at a **lower opportunity cost**.

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## Trade and prosperity

> The economics of trade

- ★ What if a country is **better** in the production of **both** goods?:
  - ▶ Singapore can produce either **100 units of banking** OR **50 units of tourism** per year
  - ▶ Cyprus can produce either **50 units of banking** OR **40 units of tourism** per year.
- ★ If countries rely on **autarky** (splitting their resources 50-50):
  - ▶ Singapore can produce **50** and **25**
  - ▶ Cyprus can produce **25** and **20** } **Total 75** and **45** will be produced.
- ★ If countries **trade**:
  - ▶ Singapore can produce **80** and **10**
  - ▶ Cyprus can produce **0** and **40** } **Total 80** and **50** will be produced.

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## Inequality

> Inequality

- ★ In general, trade allows for a **larger pie** to be distributed:
  - ▶ In the L-R, **more winners** than losers
  - ▶ In the S-R, there can be a **significant number of losers**.
- ★ For **instance**, when **China** opened up in 1989:
  - ▶ It made the West **richer on average**
  - ▶ But brought **unemployment** to some local communities
  - ▶ Costs and benefits of globalization were **NOT distributed equally**.

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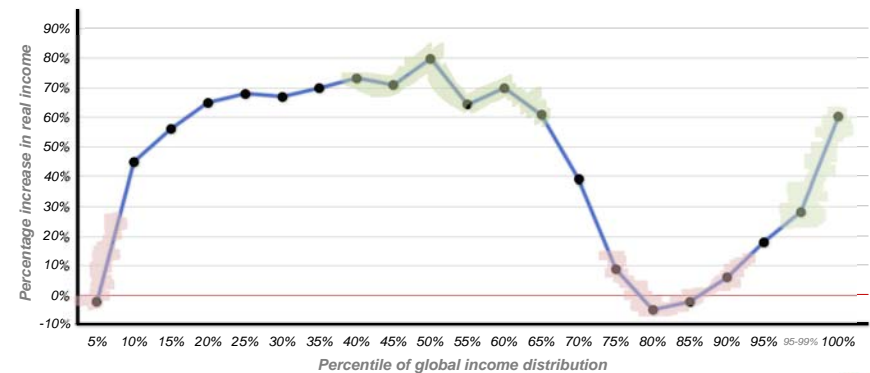
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## The Lakner-Milanovic curve (1988 – 2008)

> Inequality



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## Political change

> Inequality

- ★ It was the latter group that got disappointed, turned **against globalization** and **drove** the recent political turn towards “economic nationalism”  
Donald Trump, Brexit, radical parties gained power in Europe.

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## Should we roll back globalization?

> Inequality

- ★ Globalization undoubtedly **has contributed** to inequality  
**BUT technology** also brings inequality, yet **nobody** demands to roll it back!
- ★ Reversing globalization will bring an **all-new social shock**:
  - ▶ **Tariffs** on goods may have unpredictable reverse effects
  - ▶ **Communities** have adapted (factories closed, technologies evolved, people left).
- ★ We could have **mitigated** the adverse effects with **policies**:  
public goods, social safety nets, reskilling
- ★ But its always easier to **put the blame** on those on the other side of the border  
especially when they are of slightly **different color, religion** or **culture** than us.

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The end!

*(you are welcomed to stay for consultation or discussion)*

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