

**Chapter 9: Application: International Trade**  
**Principles of Economics, 8<sup>th</sup> Edition**  
**N. Gregory Mankiw**  
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1. Introduction
  - a. *This is an important chapter for understanding the world in which we live.*
  - b. All countries can benefit from trading with one another because trade allows each country to specialize in doing what it does best.
  - c. *Mankiw talks about Chapter 3 that develops the concept of comparative advantage.*
    - i. *Comparative advantage just means that each country (or a person for that matter) is a relatively lower cost producer of something.*
  
2. The Determinants of Trade
  - a. Countries benefit from specializing in the production of goods for which they have a comparative advantage.
  - b. The Equilibrium Without Trade
    - i. **Figure 1: The Equilibrium without International Trade. P. 168.**
  - c. The World Price and Comparative Advantage
    - i. The world price is the price of a good that prevails in the world for that good. P. 169.
    - ii. When the world price differs from the domestic price there are gains from trade.
  
3. The Winners and Losers from Trade
  - a. *Mankiw assumes that the country being observed is a “small country” but most countries are price takers as far as their effect on international prices.*
  - b. The Gains and Losses of an Exporting Country
    - i. Producers are better off and the consumers are worse off, but overall the country is better off.
    - ii. **Figure 2: International Trade in an Exporting Country. P. 170.**
  - c. The Gains and Losses of an Importing Country
    - i. The consumers are better off and the producers are worse off, but overall the country is better off.
    - ii. *Because producers are more focused than consumers, support for increasing imports is much weaker than for increasing exports.*
    - iii. **Figure 3: International Trade in an Importing Country. P. 172.**
  - d. The Effects of a Tariff
    - i. A tariff has two effects:
      - (1) The price and domestic production increase.
      - (2) The higher price reduces domestic consumption.
    - ii. The country is worse off because of the deadweight losses.
    - iii. Tariff is a tax on goods produced abroad and sold domestically. P.

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  - iv. **Figure 4: The Effects of a Tariff. P. 174.**
  - v. **FYI: Import Quotas: Another Way to Restrict Trade, P. 175.**
    - (1) While a tariff generates income for the government, a quota benefits the group that gets the quota.
  - e. The Lessons for Trade Policy
    - i. Educating the President about free trade.
  - f. Other Benefits of International Trade
    - i. Increased variety of goods
    - ii. Lower costs through economies of scale
    - iii. Increased competition and
    - iv. Enhanced flow of ideas.
  - g. **In the News: Trade as a Tool for Economic Development, P. 177.**
4. The Arguments for Restricting Trade
- a. The Jobs Argument
    - i. *Always be careful about arguments based on creating (or destroying) jobs.*
      - (1) *Were the workers just standing around before?*
      - (2) *Labor markets tend to clear in most industrial countries, so the better argument is that a policy increases the demand for labor and, therefore, the wages that workers can command.*
      - (3) *With trade, workers will tend to shift toward the production of goods for which the country has a comparative advantage which means that the workers should be more productive and able to command a higher wage.*
    - ii. *Some argue that everything can be produced more cheaply abroad.*
      - (1) *This ignores the effect of exchange rates.*
      - (2) *If we buy more goods from China, we increase the demand for their currency causing its value to rise and ours to fall.*
      - (3) *This eventually makes additional goods from there too expensive.*
    - iii. **In the News: Should the Winners from Free Trade Compensate the Losers?, P. 179.**
      - (1) Protectionism is like extortion.
  - b. The National Security Argument
    - i. *In most cases, this argument is used to protect a domestic industry rather than to pursue a true national security interest.*
    - ii. *Ever hear of the Jones Act that protects the US merchant marine in the name of national security?*
    - iii. Less educated workers in high wage countries are hurt by trade.
  - c. The Infant Industry Argument

