International Trade

International Trade: Causes and Consequences

An Empirical and Theoretical Text

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This book is dedicated to my mother, with fond memories

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Preface

We ought to be neither like spiders which spin things out from their insides nor like ants which merely collect but like bees which both collect and arrange.

Sir Francis Bacon (1561–1626)

With the wisdom encapsulated in Bacon's saying as the guiding principle of this book, I endeavour to incorporate the above maxim by placing equal emphasis on the theories of international trade and their empirical tests.

I have been teaching international trade as part of an international economics module since the early 1970s. The body of knowledge in both international trade and international money has expanded rapidly during the last twenty-five years. As a consequence, it has become increasingly difficult to cover the apposite contents of both trade theory and international money in one book. This is reflected in the currently used textbooks in international economics, where either the empirical studies in trade theory or the new trade theories of the 1980s usually receive perfunctory treatment. It probably is the right time to accept the natural line of division between trade theory and international money and to teach these subjects as separate modules with the intellectual rigour each subject area richly deserves.

The objective of this book is to bring together theoretical and empirical studies scattered over the pages of learned journals and books, in a manner which emphasises the tenets of economic methodology. It is useless to have some abstract economic theories if these cannot be applied to analyse the real world problems. Therefore, it is as important to study the empirical work in trade theory in rigorous detail as it is to learn the abstract trade theories in rigorous depth. In this book a theory is followed by its empirical tests in strict accordance with economic methodology.

The theoretical exposition is carried out in terms of both geometry and mathematical functions. It is well known that trade theories use fairly complicated diagrams; and a diagram can be a very powerful tool of analysis. Mathematical models are mostly counterparts of geometrical analysis, and a reader can skip the mathematical models if he or she so chooses, without any loss of orthodox theoretical knowledge. But there are exceptions. The model which deals with dynamic capital accumulation and the models which deal with endogenous growth cannot be understood without some knowledge of calculus and differential equations. I should also mention that without some mathematical knowledge it will be difficult to

understand the new models dealing with intra-industry trade and the dynamic models dealing with process and product innovations.

The book is aimed at Final Year BA/BSc undergraduate students but the MA/MSc graduate students will also benefit from it. The reader's knowledge of microeconomics and econometrics is assumed to be of Year 2 undergraduate level. The mathematical models can be understood if the reader is familiar with calculus and matrix algebra. A reader with Year 2 level of mathematics for economists should be able to cope fairly easily. It is obvious from the various new developments in trade theory that one has to have knowledge of intermediate level microeconomics, mathematics for economists, and econometrics in order to achieve a clear understanding of the empirical and theoretical work in modern trade theory.

This book can be used either to teach the trade part of international economics or to teach a full module in international trade. Chapter 1 suggests how to do this with a menu of choices of chapters and sections.

I would like to take this opportunity to thank my colleagues Paul Dunne, Len Gomes, Alan Gully, Harry Hillier and Dirk Willenbockel for useful discussions. I also wish to thank Alan Winters who commented on some of the earlier chapters and Peter Sinclair who commented on some of the later chapters. I found their comments very useful. I am most grateful to Chris Milner who patiently read the whole manuscript and sent comments and suggestions which led to definite improvements in several chapters. Needless to add, I am solely responsible for errors and omissions that may remain in the book. I have reproduced verbatim two small theorems, namely, the Dixit–Norman theorem and the Kemp–Wan theorem. I am grateful to the authors and to Cambridge University Press for granting permission for the former, and to Elsevier Science for the latter. I also wish to thank Andrew Ramsden for research assistance; and Dina Junior Manda for word-processing the final manuscript.

Last but not least, I wish to express my gratitude to my wife and my children for their love, support and patience during the long periods of enforced isolation that was necessary to complete this book.

J. BORKAKOTI