

	Contents	vii
	Preface	xx
1	Introduction	1
Part 1	International Trade Theory	9
2	World Trade: An Overview	10
3	Labor Productivity and Comparative Advantage: The Ricardian Model	24
4	Resources, Comparative Advantage, and Income Distribution	50
5	The Standard Trade Model	84
6	Economies of Scale, Imperfect Competition, and International Trade	110
7	International Factor Movements	148
Part 2	International Trade Policy	175
8	The Instruments of Trade Policy	176
9	The Political Economy of Trade Policy	207
10	Trade Policy in Developing Countries	243
11	Controversies in Trade Policy	259
Part 3	Exchange Rates and Open-Economy Macroeconomics	277
12	National Income Accounting and the Balance of Payments	278
13	Exchange Rates and the Foreign Exchange Market: An Asset Approach	306
14	Money, Interest Rates, and Exchange Rates	338
15	Price Levels and the Exchange Rate in the Long Run	369
16	Output and the Exchange Rate in the Short Run	407
17	Fixed Exchange Rates and Foreign Exchange Intervention	447
Part 4	International Macroeconomic Policy	485
18	The International Monetary System, 1870–1973	486
19	Macroeconomic Policy and Coordination Under Floating Exchange Rates	516
20	Optimum Currency Areas and the European Experience	548
21	The Global Capital Market: Performance and Policy Problems	576
22	Developing Countries: Growth, Crisis, and Reform	602

Mathematical Postscripts	641
Postscript to Chapter 4: The Factor Proportions Model	642
Postscript to Chapter 5: The Trading World Economy	646
Postscript to Chapter 6: The Monopolistic Competition Model	655
Postscript to Chapter 21: Risk Aversion and International Portfolio Diversification	657
Credits	664
Index	665

Preface	xx
---------------	----

1 Introduction	1
What Is International Economics About?	3
The Gains from Trade	3
The Pattern of Trade	5
How Much Trade?	5
Balance of Payments	6
Exchange Rate Determination	6
International Policy Coordination	7
The International Capital Market	7
International Economics: Trade and Money	8

Part 1 International Trade Theory	9
--	----------

2 World Trade: An Overview	10
Who Trades with Whom?	11
Size Matters: The Gravity Model	11
The Logic of the Gravity Model	13
Using the Gravity Model: Looking for Anomalies	14
Impediments to Trade: Distance, Barriers, and Borders	15
The Changing Pattern of World Trade	17
Has the World Gotten Smaller?	17
What Do We Trade?	19
Multinational Corporations and Outsourcing	20
Do Old Rules Still Apply?	21
Summary	22

3 Labor Productivity and Comparative Advantage:	
The Ricardian Model	24
The Concept of Comparative Advantage	25
A One-Factor Economy	26
Production Possibilities	26
Relative Prices and Supply	27
Trade in a One-Factor World	28
Determining the Relative Price After Trade	29
BOX: Comparative Advantage in Practice: The Case of Babe Ruth	31
The Gains from Trade	33
A Numerical Example	34
Relative Wages	35
BOX: The Losses from Nontrade	36
Misconceptions About Comparative Advantage	36
Productivity and Competitiveness	37
The Pauper Labor Argument	37
BOX: Do Wages Reflect Productivity?	38
Exploitation	39
Comparative Advantage with Many Goods	40
Setting Up the Model	40

Relative Wages and Specialization	40
Determining the Relative Wage in the Multigood Model	42
Adding Transport Costs and Nontraded Goods	43
Empirical Evidence on the Ricardian Model	45
Summary	47

4 Resources, Comparative Advantage, and Income Distribution

50

A Model of a Two-Factor Economy	51
Prices and Production	51
Choosing the Mix of Inputs	54
Factor Prices and Goods Prices	55
Resources and Output	57
Effects of International Trade Between Two-Factor Economies	61
Relative Prices and the Pattern of Trade	61
Trade and the Distribution of Income	63
Factor-Price Equalization	64
Trade and Income Distribution in the Short Run	66
CASE STUDY: North-South Trade and Income Inequality	66
The Political Economy of Trade: A Preliminary View	68
The Gains from Trade, Revisited	68
Optimal Trade Policy	70
Income Distribution and Trade Politics	71
Empirical Evidence on the Heckscher-Ohlin Model	71
BOX: Income Distribution and the Beginnings of Trade Theory	72
Testing the Heckscher-Ohlin Model	72
Implications of the Tests	76
Summary	76
Appendix: Factor Prices, Goods Prices, and Input Choices	80
Choice of Technique	80
Goods Prices and Factor Prices	82

5 The Standard Trade Model

84

A Standard Model of a Trading Economy	85
Production Possibilities and Relative Supply	85
Relative Prices and Demand	86
The Welfare Effect of Changes in the Terms of Trade	89
Determining Relative Prices	89
Economic Growth: A Shift of the <i>RS</i> curve	89
Growth and the Production Possibility Frontier	90
Relative Supply and the Terms of Trade	91
International Effects of Growth	92
CASE STUDY: Has the Growth of Newly Industrializing Countries Hurt Advanced Nations?	93
International Transfers of Income: Shifting the <i>RD</i> Curve	95
The Transfer Problem	95
Effects of a Transfer on the Terms of Trade	96
Presumptions About the Terms of Trade Effects of Transfers	97
CASE STUDY: The Transfer Problem and the Asian Crisis	98
Tariffs and Export Subsidies: Simultaneous Shifts in <i>RS</i> and <i>RD</i>	99
Relative Demand and Supply Effects of a Tariff	99
Effects of an Export Subsidy	100

Implications of Terms of Trade Effects: Who Gains and Who Loses?	101
Summary	103
Appendix: Representing International Equilibrium with Offer Curves	107
Deriving a Country's Offer Curve	107
International Equilibrium	108

6 Economies of Scale, Imperfect Competition, and International Trade 110

Economies of Scale and International Trade: An Overview	111
Economies of Scale and Market Structure	112
The Theory of Imperfect Competition	113
Monopoly: A Brief Review	113
Monopolistic Competition	116
Limitations of the Monopolistic Competition Model	120
Monopolistic Competition and Trade	121
The Effects of Increased Market Size	121
Gains from an Integrated Market: A Numerical Example	123
Economies of Scale and Comparative Advantage	125
The Significance of Intraindustry Trade	128
Why Intraindustry Trade Matters	129
CASE STUDY: Intraindustry Trade in Action:	
The North American Auto Pact of 1964	130
Dumping	131
The Economics of Dumping	131
CASE STUDY: Antidumping as Protectionism	134
Reciprocal Dumping	135
The Theory of External Economies	136
Specialized Suppliers	136
Labor Market Pooling	137
Knowledge Spillovers	138
External Economies and Increasing Returns	139
External Economies and International Trade	139
External Economies and the Pattern of Trade	139
Trade and Welfare with External Economies	140
Dynamic Increasing Returns	141
BOX: Tinseltown Economics	143
Summary	143
Appendix: Determining Marginal Revenue	147

7 International Factor Movements 148

International Labor Mobility	149
A One-Good Model Without Factor Mobility	149
International Labor Movement	151
Extending the Analysis	152
CASE STUDY: Wage Convergence in the Age of Mass Migration	153
CASE STUDY: Immigration and the U.S. Economy	154
International Borrowing and Lending	155
Intertemporal Production Possibilities and Trade	155
The Real Interest Rate	156
Intertemporal Comparative Advantage	157
Direct Foreign Investment and Multinational Firms	157

BOX: Does Capital Movement to Developing Countries Hurt

Workers in High-Wage Countries?	158
The Theory of Multinational Enterprise	159
Multinational Firms in Practice	161
CASE STUDY: Foreign Direct Investment in the United States	162
BOX: Taken for a Ride?	164
Summary	164
Appendix 1: Finding Total Output from the Marginal Product Curve	168
Appendix 2: More on Intertemporal Trade	170

Part 2	International Trade Policy	175
---------------	-----------------------------------	------------

8	The Instruments of Trade Policy	176
----------	--	------------

Basic Tariff Analysis	176
Supply, Demand, and Trade in a Single Industry	177
Effects of a Tariff	179
Measuring the Amount of Protection	180
Costs and Benefits of a Tariff	182
Consumer and Producer Surplus	182
Measuring the Costs and Benefits	184
Other Instruments of Trade Policy	186
Export Subsidies: Theory	186
CASE STUDY: Europe's Common Agricultural Policy	187
Import Quotas: Theory	188
CASE STUDY: An Import Quota in Practice: U.S. Sugar	190
Voluntary Export Restraints	191
CASE STUDY: A Voluntary Export Restraint in Practice:	
Japanese Autos	192
Local Content Requirements	193
Other Trade Policy Instruments	193
BOX: American Buses, Made in Hungary	194
The Effects of Trade Policy: A Summary	194
Summary	195
Appendix 1: Tariff Analysis in General Equilibrium	199
A Tariff in a Small Country	199
A Tariff in a Large Country	201
Appendix 2: Tariffs and Import Quotas in the Presence of Monopoly	203
The Model with Free Trade	203
The Model with a Tariff	204
The Model with an Import Quota	205
Comparing a Tariff and a Quota	205

9	The Political Economy of Trade Policy	207
----------	--	------------

The Case for Free Trade	208
Free Trade and Efficiency	208
Additional Gains from Free Trade	209
Political Argument for Free Trade	210
CASE STUDY: The Gains from 1992	211
National Welfare Arguments Against Free Trade	213
The Terms of Trade Argument for a Tariff	213
The Domestic Market Failure Argument Against Free Trade	214
How Convincing Is the Market Failure Argument?	216

Income Distribution and Trade Policy	217
Electoral Competition	218
Collective Action	219
BOX: Politicians for Sale: Evidence from the 1990s	220
Modeling the Political Process	220
Who Gets Protected?	221
International Negotiations and Trade Policy	223
The Advantages of Negotiation	224
International Trade Agreements: A Brief History	225
The Uruguay Round	227
Trade Liberalization	227
From the GATT to the WTO	228
Benefits and Costs	229
BOX: Settling a Dispute—and Creating One	230
CASE STUDY: Testing the WTO's Metal	231
Preferential Trading Agreements	232
BOX: Free Trade Area versus Customs Union	233
BOX: Do Trade Preferences Have Appeal?	234
CASE STUDY: Trade Diversion in South America	235
Summary	236
Appendix: Proving that the Optimum Tariff Is Positive	240
Demand and Supply	240
The Tariff and Prices	240
The Tariff and Domestic Welfare	241

10 Trade Policy in Developing Countries 243

Import-Substituting Industrialization	244
The Infant Industry Argument	244
Promoting Manufacturing Through Protection	246
CASE STUDY: The End of Import Substitution in Chile	248
Results of Favoring Manufacturing: Problems of	
Import-Substituting Industrialization	248
Trade Liberalization Since 1985	250
Export-Oriented Industrialization: The East Asian Miracle	252
The Facts of Asian Growth	252
Trade Policy in the HPAEs	253
BOX: China's Boom	254
Industrial Policy in the HPAEs	255
Other Factors in Growth	256
Summary	256

11 Controversies in Trade Policy 259

Sophisticated Arguments for Activist Trade Policy	260
Technology and Externalities	260
Imperfect Competition and Strategic Trade Policy	262
CASE STUDY: When the Chips Were Up	265
Globalization and Low-Wage Labor	267
The Anti-Globalization Movement	267
Trade and Wages Revisited	268
Labor Standards and Trade Negotiations	270
Environmental and Cultural Issues	270
The WTO and National Independence	271

CASE STUDY: The Shipbreakers of Alang	272
Summary	273

Part 3	Exchange Rates and Open-Economy Macroeconomics	277
---------------	---	------------

12	National Income Accounting and the Balance of Payments	278
-----------	---	------------

The National Income Accounts	280
National Product and National Income	281
Capital Depreciation, International Transfers, and Indirect Business Taxes	282
Gross Domestic Product	282
National Income Accounting for an Open Economy	283
Consumption	283
Investment	283
Government Purchases	284
The National Income Identity for an Open Economy	284
An Imaginary Open Economy	285
The Current Account and Foreign Indebtedness	285
Saving and the Current Account	287
Private and Government Saving	288

CASE STUDY: Government Deficit Reduction May Not Increase the

Current Account Surplus	289
The Balance of Payments Accounts	291
Examples of Paired Transactions	292
The Fundamental Balance of Payments Identity	294
The Current Account, Once Again	294
The Capital Account	296
The Financial Account	296
The Statistical Discrepancy	297
Official Reserve Transactions	297

CASE STUDY: The Assets and Liabilities of the World's Biggest Debtor

Summary	302
---------------	-----

13	Exchange Rates and the Foreign Exchange Market: An Asset Approach	306
-----------	--	------------

Exchange Rates and International Transactions	307
Domestic and Foreign Prices	307
Exchange Rates and Relative Prices	309
The Foreign Exchange Market	310
The Actors	310
Characteristics of the Market	311
BOX: A Tale of Two Dollars	312
Spot Rates and Forward Rates	314
Foreign Exchange Swaps	316
Futures and Options	316
The Demand for Foreign Currency Assets	316
Assets and Asset Returns	317
Risk and Liquidity	318
Interest Rates	318
Exchange Rates and Asset Returns	319
A Simple Rule	321
Return, Risk, and Liquidity in the Foreign Exchange Market	322

Equilibrium in the Foreign Exchange Market	323
Interest Parity: The Basic Equilibrium Condition	323
How Changes in the Current Exchange Rate Affect Expected Returns	324
The Equilibrium Exchange Rate	326
Interest Rates, Expectations, and Equilibrium	328
The Effect of Changing Interest Rates on the Current Exchange Rate	328
The Effect of Changing Expectations on the Current Exchange Rate	330
Summary	330
Appendix: Forward Exchange Rates and Covered Interest Parity	335

14 Money, Interest Rates, and Exchange Rates 338

Money Defined: A Brief Review	339
Money as a Medium of Exchange	339
Money as a Unit of Account	339
Money as a Store of Value	340
What Is Money?	340
How the Money Supply Is Determined	340
The Demand for Money by Individuals	341
Expected Return	341
Risk	342
Liquidity	342
Aggregate Money Demand	342
The Equilibrium Interest Rate: The Interaction of Money	
Supply and Demand	343
Equilibrium in the Money Market	344
Interest Rates and the Money Supply	346
Output and the Interest Rate	347
The Money Supply and the Exchange Rate in the Short Run	347
Linking Money, the Interest Rate, and the Exchange Rate	348
U.S. Money Supply and the Dollar/Euro Exchange Rate	349
Europe's Money Supply and the Dollar/Euro Exchange Rate	350
Money, the Price Level, and the Exchange Rate in the Long Run	353
Money and Money Prices	353
The Long-Run Effects of Money Supply Changes	354
Empirical Evidence on Money Supplies and Price Levels	355
Money and the Exchange Rate in the Long Run	355
Inflation and Exchange Rate Dynamics	356
Short-Run Price Rigidity versus Long-Run Price Flexibility	357
BOX: Money Supply Growth and Hyperinflation in Bolivia	358
Permanent Money Supply Changes and the Exchange Rate	360
Exchange Rate Overshooting	362
CASE STUDY: Money Supplies, Expectations, and	
the Exchange Rate of the Iraqi: Dinar	363
Summary	365

15 Price Levels and the Exchange Rate in the Long Run 369

The Law of One Price	370
Purchasing Power Parity	371
The Relationship Between PPP and the Law of One Price	372
Absolute PPP and Relative PPP	372
A Long-Run Exchange Rate Model Based on PPP	373

The Fundamental Equation of the Monetary Approach	373
Ongoing Inflation, Interest Parity, and PPP	375
The Fisher Effect	376
Empirical Evidence on PPP and the Law of One Price	379
Explaining the Problems with PPP	381
Trade Barriers and Nontradables	381
BOX: Some Meaty Evidence on the Law of One Price	382
Departures from Free Competition	385
Differences in Consumption Patterns and Price Level Measurement	385
PPP in the Short Run and in the Long Run	386
CASE STUDY: Why Price Levels Are Lower in Poorer Countries	387
Beyond Purchasing Power Parity: A General Model of Long-Run Exchange Rates	389
The Real Exchange Rate	389
Demand, Supply, and the Long-Run Real Exchange Rate	391
BOX: Sticky Prices and the Law of One Price:	
Evidence from Scandinavian Duty-Free Shops	392
Nominal and Real Exchange Rates in Long-Run Equilibrium	393
International Interest Rate Differences and the Real Exchange Rate	397
Real Interest Parity	398
Summary	399
Appendix: The Fisher Effect, the Interest Rate, and the Exchange	
Rate under the Flexible-Price Monetary Approach	404

16 Output and the Exchange Rate in the Short Run	407
Determinants of Aggregate Demand in an Open Economy	408
Determinants of Consumption Demand	408
Determinants of the Current Account	409
How Real Exchange Rate Changes Affect the Current Account	410
How Disposable Income Changes Affect the Current Account	411
The Equation of Aggregate Demand	411
The Real Exchange Rate and Aggregate Demand	411
Real Income and Aggregate Demand	411
How Output Is Determined in the Short Run	412
Output Market Equilibrium in the Short Run: The DD Schedule	414
Output, the Exchange Rate, and Output Market Equilibrium	414
Deriving the DD Schedule	415
Factors That Shift the DD Schedule	415
Asset Market Equilibrium in the Short Run: The AA Schedule	418
Output, the Exchange Rate, and Asset Market Equilibrium	419
Deriving the AA Schedule	420
Factors That Shift the AA Schedule	421
Short-Run Equilibrium for an Open Economy: Putting	
the DD and AA Schedules Together	422
Temporary Changes in Monetary and Fiscal Policy	424
Monetary Policy	424
Fiscal Policy	425
Policies to Maintain Full Employment	426
Inflation Bias and Other Problems of Policy Formulation	427
Permanent Shifts in Monetary and Fiscal Policy	428
A Permanent Increase in the Money Supply	429
Adjustment to a Permanent Increase in the Money Supply	430

A Permanent Fiscal Expansion	431
Macroeconomic Policies and the Current Account	433
Gradual Trade Flow Adjustment and Current Account Dynamics	434
The J-Curve	434
BOX: Exchange Rates and the Current Account	436
Exchange Rate Pass-Through and Inflation	436
Summary	439
Appendix 1: Intertemporal Trade and Consumption Demand	442
Appendix 2: The Marshall-Lerner Condition and Empirical	
Estimates of Trade Elasticities	444

17 Fixed Exchange Rates and Foreign Exchange Intervention

447

Why Study Fixed Exchange Rates?	448
Central Bank Intervention and the Money Supply	449
The Central Bank Balance Sheet and the Money Supply	449
Foreign Exchange Intervention and the Money Supply	451
Sterilization	451
The Balance of Payments and the Money Supply	452
How the Central Bank Fixes the Exchange Rate	453
Foreign Exchange Market Equilibrium Under a Fixed Exchange Rate	453
Money Market Equilibrium Under a Fixed Exchange Rate	454
A Diagrammatic Analysis	455
Stabilization Policies with a Fixed Exchange Rate	456
Monetary Policy	456
Fiscal Policy	457
Changes in the Exchange Rate	458
Adjustment to Fiscal Policy and Exchange Rate Changes	460
Balance of Payments Crises and Capital Flight	460
Managed Floating and Sterilized Intervention	463
Perfect Asset Substitutability and the Ineffectiveness of Sterilized Intervention	463
BOX: Brazil's 1998–1999 Balance of Payments Crisis	464
Foreign Exchange Market Equilibrium Under Imperfect Asset Substitutability	465
The Effects of Sterilized Intervention with Imperfect Asset Substitutability	466
Evidence on the Effects of Sterilized Intervention	467
Reserve Currencies in the World Monetary System	468
The Mechanics of a Reserve Currency Standard	469
The Asymmetric Position of the Reserve Center	470
The Gold Standard	470
The Mechanics of a Gold Standard	470
Symmetric Monetary Adjustment Under a Gold Standard	471
Benefits and Drawbacks of the Gold Standard	472
The Bimetallic Standard	473
The Gold Exchange Standard	473
Summary	474
Appendix 1: Equilibrium in the Foreign Exchange Market	
with Imperfect Asset Substitutability	479
Demand	479
Supply	480
Equilibrium	480
Appendix 2: The Timing of Balance of Payments Crises	482

18 The International Monetary System, 1870–1973 486

Macroeconomic Policy Goals in an Open Economy	487
Internal Balance: Full Employment and Price Level Stability	487
External Balance: The Optimal Level of the Current Account	488
International Macroeconomic Policy Under the Gold Standard, 1870–1914	491
Origins of the Gold Standard	491
External Balance Under the Gold Standard	491
The Price-Specie-Flow Mechanism	492
The Gold Standard “Rules of the Game”: Myth and Reality	493
Internal Balance Under the Gold Standard	493
BOX: Hume versus the Mercantilists	494
CASE STUDY: The Political Economy of Exchange Rate Regimes:	
Conflict Over America’s Monetary Standard During the 1890s	495
The Interwar Years, 1918–1939	496
The Fleeting Return to Gold	496
International Economic Disintegration	497
CASE STUDY: The International Gold Standard and the Great Depression	498
The Bretton Woods System and the International Monetary Fund	499
Goals and Structure of the IMF	499
Convertibility and the Expansion of Private Financial Flows	500
Speculative Financial Flows and Crises	501
Analyzing Policy Options Under the Bretton Woods System	502
Maintaining Internal Balance	502
Maintaining External Balance	503
Expenditure-Changing and Expenditure-Switching Policies	504
The External Balance Problem of the United States	506
CASE STUDY: The Decline and Fall of the Bretton Woods System	507
Worldwide Inflation and the Transition to Floating Rates	510
Summary	513

19 Macroeconomic Policy and Coordination Under Floating Exchange Rates 516

The Case for Floating Exchange Rates	517
Monetary Policy Autonomy	517
Symmetry	518
Exchange Rates as Automatic Stabilizers	519
The Case Against Floating Exchange Rates	521
Discipline	521
Destabilizing Speculation and Money Market Disturbances	522
Injury to International Trade and Investment	522
Uncoordinated Economic Policies	523
The Illusion of Greater Autonomy	523
CASE STUDY: Exchange Rate Experience Between the Oil	
Shocks, 1973–1980	524
Macroeconomic Interdependence Under a Floating Rate	528
CASE STUDY: Disinflation, Growth, Crisis, and Recession, 1980–2005	529
What Has Been Learned Since 1973?	533
Monetary Policy Autonomy	533
BOX: Why Has Asia Sustained America’s Record Current Account Deficits?	534
Symmetry	537

The Exchange Rate as an Automatic Stabilizer	537
Discipline	538
Destabilizing Speculation	538
International Trade and Investment	539
Policy Coordination	540
Are Fixed Exchange Rates Even an Option for Most Countries?	540
Directions for Reform	541
Summary	541
Appendix: International Policy Coordination Failures	545

20 Optimum Currency Areas and the European Experience 548

How the European Single Currency Evolved	549
What Has Driven European Monetary Cooperation?	550
The European Monetary System, 1979–1998	551
German Monetary Dominance and the Credibility Theory of the EMS	552
The EU “1992” Initiative	522
European Economic and Monetary Union	554
The Euro and Economic Policy in the Euro Zone	555
The Maastricht Convergence Criteria and the Stability and Growth Pact	555
The European System of Central Banks	556
BOX: Designing and Naming a New Currency	557
The Revised Exchange Rate Mechanism	558
The Theory of Optimum Currency Areas	558
Economic Integration and the Benefits of a Fixed	
Exchange Rate Area: The <i>GG</i> Schedule	559
Economic Integration and the Costs of a Fixed	
Exchange Rate Area: The <i>LL</i> Schedule	560
The Decision to Join a Currency Area: Putting the <i>GG</i> and <i>LL</i> Schedules Together	562
What Is an Optimum Currency Area?	564
CASE STUDY: Is Europe an Optimum Currency Area?	565
The Future of EMU	569
BOX: How Much Trade Do Currency Unions Create?	570
Summary	572

21 The Global Capital Market: Performance and Policy Problems 576

The International Capital Market and the Gains from Trade	577
Three Types of Gain from Trade	577
Risk Aversion	578
Portfolio Diversification as a Motive for International Asset Trade	579
The Menu of International Assets: Debt versus Equity	580
International Banking and the International Capital Market	580
The Structure of the International Capital Market	581
Growth of the International Capital Market	581
Offshore Banking and Offshore Currency Trading	582
The Growth of Eurocurrency Trading	583
The Importance of Regulatory Asymmetries	584
Regulating International Banking	585
The Problem of Bank Failure	585
Difficulties in Regulating International Banking	587

International Regulatory Cooperation	588
CASE STUDY: The Day the World Almost Ended	589
How Well Has the International Capital Market Performed?	591
The Extent of International Portfolio Diversification	592
The Extent of Intertemporal Trade	593
Onshore-Offshore Interest Differentials	594
The Efficiency of the Foreign Exchange Market	595
Summary	598

22 Developing Countries: Growth, Crisis, and Reform 602

Income, Wealth, and Growth in the World Economy	603
The Gap Between Rich and Poor	603
Has the World Income Gap Narrowed Over Time?	604
Structural Features of Developing Countries	606
Developing-Country Borrowing and Debt	609
The Economics of Financial Inflows to Developing Countries	609
The Problem of Default	610
Alternative Forms of Financial Inflow	612
The Problem of "Original Sin"	614
The Debt Crisis of the 1980s	614
Reforms, Capital Inflows, and the Return of Crisis	615
BOX: The Simple Algebra of Moral Hazard	619
East Asia: Success and Crisis	619
The East Asian Economic Miracle	619
Asian Weaknesses	620
BOX: What Did East Asia Do Right?	621
The Asian Financial Crisis	622
Spillover to Russia	624
CASE STUDY: Can Currency Boards Make Fixed Exchange Rates Credible?	625
Lessons of Developing Country-Crises	627
Reforming the World's Financial "Architecture"	629
Capital Mobility and the Trilemma of the Exchange Rate Regime	629
"Prophylactic" Measures	632
Coping with Crisis	633
A Confused Future	633
Understanding Global Capital Flows and the Global	
Distribution of Income: Is Geography Destiny?	633
Summary	637

Mathematical Postscripts 641

Postscript to Chapter 4: The Factor Proportions Model	642
Factor Prices and Costs	642
The Basic Equations in the Factor Proportions Model	643
Goods Prices and Factor Prices	644
Factor Supplies and Outputs	645
Postscript to Chapter 5: The Trading World Economy	646
Supply, Demand, and Equilibrium	646
World Equilibrium	646
Production and Income	646
Income, Prices, and Utility	647
Supply, Demand, and the Stability of Equilibrium	648

Effects of Changes in Supply and Demand	650
The Method of Comparative Statics	650
Economic Growth	651
The Transfer Problem	652
A Tariff	653
Postscript to Chapter 6: The Monopolistic Competition Model	655
Postscript to Chapter 21: Risk Aversion and International	657
Portfolio Diversification	657
An Analytical Derivation of the Optimal Portfolio	657
A Diagrammatic Derivation of the Optimal Portfolio	658
The Effects of Changing Rates of Return	660
 Credits	 664
Index	665