FACULTY AND CONTACT INFORMATION

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Office hours: Friday 1:30-3:00PM and by appointment
Class hours: Tuesday 5:00-8:20
Classroom: VKC 260

COURSE SCOPE AND OBJECTIVE

This course provides a systematic understanding of critical aspects of international trade and finance. The course is divided in three sections. The first and second sections deal with international trade. The third section deals with international finance.

International trade is one of the important forces driving toward globalization, that is, the integration of national business activities into globally competitive markets. The first section of the course examines the role of comparative advantage as a determinant of the location of production and review several theories that explain why countries trade with each other. The second section examines the effects of government policies toward international trade with special attention to trade tariffs, quotas, voluntary export restrictions and subsidies. Another goal of this section is to study the economic and political forces underlying the creation of trade blocs such as free trade areas, custom unions and common markets.

The third section of the course deals with international finance which is another important force driving toward globalization. This section examines how international financial markets operate and the forces driving toward the globalization of these markets. Central to the analysis is the role of money in an international context and the role of exchange rates as relative prices of national currencies. The course develops some key principles of international financial investment and examines how the foreign exchange can be used to hedge and speculate in financial markets. It also studies the role of government policies toward the foreign exchange market, including the choice
between fixed and floating exchange rates, and the use of exchange controls to create impediments to excess currency volatility. This section will also study the dynamics of financial and currency crises.

**Learning objectives**

The primary objective of this course is to enable you to make informed judgments about the consequences of increasing worldwide integration in trade and finance. Knowing the consequence of trade and financial integration is important for making informed business decisions. Achieving this goal involves several steps. First, you must become familiar with the main empirical facts and trends about the process of trade and financial integration. Second, you must learn why we observe these trends (theoretical explanations). An understanding of the trade and international finance theory is necessary for interpreting the empirical dynamics of trade and financial variables. Third, you must learn how the institutional environment of the countries participating in the globalization process and their government policies affect the process of trade and financial integration and, ultimately, the well-being of the participating countries.

**COURSE MATERIALS**

- **Slides**: I will post in Blackboard the slides for each topic before the first class session dealing with the particular topic.
- **Additional readings**: Later in the course I will post some readings in Blackboard.

I strongly recommend to read (perhaps quickly) the book sections indicated in the list of topics below before the class meets. In class I will cover the concepts and issues that are most challenging, reinforcing and extending what is in the required reading. I also suggest that after the class session you review the reading to solidify your understanding.

It is important that you develop the ability to use and apply the concepts and tools developed in the course. The best way to do this is by practicing actively. Questions and problems in the textbooks are one source of practice items.

**COURSE REQUIREMENTS AND GRADING**

The course grade will be based on the following weighted requirements:

1. First mid-term examination 25%
2. Second mid-term examination 25%
3. Final examination 27%
4. Six problem sets 12%
5. One group assignment 8%
6. Class attendance, participation and presentation 3%
The two midterm exams and the final exam are not cumulative and will address the subject matter that precedes them. For all the exams, you are responsible for the assigned textbook chapters, any material covered in class. The exams are intended to assess how well you understand the basic ideas and principles. All exams are closed-book, closed notes. You may use a calculator but not a cell phone, laptop, or any other electronic device.

The group assignment will be posted in Blackboard one month before the project is due. A group can contain between 2 and 4 students. It cannot contain more than 4 members. Students are encouraged to form their own group. Those who do not form a group by themselves will be assignment to additional groups randomly.

It is highly recommended to keep up with current developments in the international environment, both for class purposes and for your own benefit. You can do this by reading the relevant articles in newspapers (e.g., Financial Times, Wall Street Journal, New York Times) or weekly magazine (e.g., the Economist). To encourage the readings of news and the applications of theory to the real world, students are encouraged to make in-class presentations of issues recently covered in the news that are related to the topics of the course. We will use the last 15 minutes of class for these presentations and they contribute to their class participation. The presentation can be done in groups of 2, 3 or 4 students. The groups can be the same as the ones for the group assignment as described above.

Each individual course requirement receives a numerical score but not a letter grade. The overall numerical score in the course is converted into a letter grade at the end of the semester in accordance with the Marshall School guidelines. There is no official quota for the number of A’s, B’s, etc., although the average grade for elective undergraduate courses can be expected to be close to 3.3 (corresponding to a B+) out of 4.0.

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EXPECTATIONS AND CLASSROOM ETIQUETTE

It is very important that you contribute to the interactive nature of the classroom environment. Although all class sessions will be conducted in lecture format, classroom interaction is highly encouraged. I especially encourage active participation in the discussion through observations and questions. And I also expect many questions from students. No laptops or other internet access devices can be used in class.

ACADEMIC CONDUCT

Plagiarism—presenting someone else’s ideas as your own, either verbatim or recast in your own words—is a serious academic offense with serious consequences. Please familiarize yourself with the discussion of plagiarism in SCampus in Section 11, Behavior Violating University Standards https://scampus.usc.edu/1100-behavior-violating-university-standards-and-appropriate-sanctions. Other forms of academic dishonesty are equally unacceptable. See additional information in SCampus and university policies on scientific misconduct, http://policy.usc.edu/scientific-misconduct.

Discrimination, sexual assault, and harassment are not tolerated by the university. You are encouraged to report any incidents to the Office of Equity and Diversity http://equity.usc.edu or to the Department of Public Safety http://capsnet.usc.edu/department/department-public-safety/online-forms/contact-us. This is important for the safety of the whole USC community. Another member of the university community—such as a friend, classmate, advisor, or faculty member—can help initiate the report, or can initiate the report on behalf of another person. The Center for Women and Men http://www.usc.edu/student-affairs/cwm/ provides 24/7 confidential support, and the sexual assault resource center webpage http://sarc.usc.edu describes reporting options and other resources.

SUPPORT SYSTEM

Students whose primary language is not English should check with the American Language Institute http://dornsife.usc.edu/ali, which sponsors courses and workshops specifically for international graduate students. The Office of Disability Services and Programs www.usc.edu/disability provides certification for students with disabilities and helps arrange the relevant accommodations. If an officially declared emergency makes travel to campus infeasible, USC Emergency Information http://emergency.usc.edu will provide safety and other updates, including ways in which instruction will be continued by means of blackboard, teleconferencing, and other technology.
PART I: THEORIES OF INTERNATIONAL TRADE

1. (Jan. 13) - Introduction: International Linkages and Globalization. Basic Theory Using Demand and Supply

   Industry demand and consumer surplus.
   Industry supply and producer surplus.
   Free trade equilibrium and the net national gains from trade.

   Required reading: Pugel, Chapter 1, 2. Practice Questions and Problems 1-12 (Chapter 2).

2. (Jan. 20) Why Countries Trade

   Adam Smith’s theory of absolute advantage.
   Ricardo’s theory of comparative advantage.
   Heckscher-Ohlin theory of factor proportions.


   Short-term welfare consequences.
   Long-term welfare consequences.
   Are the predictions of the H-O theory supported by the trade data?

   Required reading: Pugel, Chapter 5. Practice Questions and Problems: 1-6, 8-10 (Chapter 5).

4. (Feb. 3) Alternative Theories of Trade

   Increasing intra-industry trade and the limits of the Heckscher-Ohlin’s theory.
   Economies of scale.
   Monopolistic competition.
   Oligopoly and international trade.
   External scale economies.

   Required reading: Pugel, Chapter 6. Practice Questions and Problems: 1-10 (Chapter 6).

5. First midterm exam covering Part I only (Feb. 10)
PART II: TRADE POLICIES

6. The Analysis of Tariffs (Feb. 17)

The effects of tariffs on producers, consumers and government revenues.
The net national consequences of tariffs.
The nationally optimal tariff.

Required reading: Pugel, Chapter 8.
Practice Questions and Problems: 1-8 (Chapter 8).

7. Nontariff Barriers to Imports (Feb. 24)

Import quota
Import quotas versus tariffs
Voluntary export restraints (VERs)
Other nontariff barriers
The real world is not first best.

Required reading: Pugel, Chapter 9, 10.
Practice Questions and Problems: 1-9 (Chapter 9).

8. Pushing Exports and migration (Mar. 3)

Dumping and antidumping policies.
Exports subsidies.
Countervailing duties.
Migration, the labor market and policies toward immigration.

Required reading: Pugel, Chapter 11, 15 (Pages 343-344, 363-374).
Practice Questions and Problems: 1-8 (Chapter 11).
Practice Questions and Problems: 10-16 (Chapter 15).

9. Trade Blocs and Trade Blocks (Mar. 10)

Free-Trade Area, Customs Unions, Common Market, Economic Union.
The theory of trade blocks: trade creation and trade diversion.
North American Free Trade Agreement (NAFTA)
Trade blocks among developing countries.
Trade embargoes.

Required reading: Pugel, Chapter 12.
Practice Questions and Problems: 1-10.
PART III: International Finance

10. **Payments among nations and foreign exchange market (Mar. 24)**

   Balance of payment.
   Current account.
   Capital account.
   Foreign reserves.
   The basic currency trading.
   Demand and supply for foreign exchange.
   Floating and fixed exchange rates.
   Arbitrage in the spot exchange market.

   *Required reading: Pugel, Chapter 16, 17*
   - Practice Questions and Problems: 1-10 (Chapter 16).
   - Practice Questions and Problems: 1-10 (Chapter 17).

11. **Forward exchange and international financial investment (Mar. 31)**

   Hedging the risk using the foreign exchange market.
   Speculating using the foreign exchange market.
   Other currency contracts: futures, options and swaps.
   International investment with and without cover.
   Covered interest arbitrage and covered interest parity.
   Does the interest rate parity hold?

   *Required reading: Pugel, Chapter 18.*
   - Practice Questions and Problems: 1-10.

12. **Second midterm exam covering Part II only (Apr. 7)**


   Exchange rates in the short and long run.
   Purchasing Power Parity (PPP): absolute and relative PPP.
   Exchange rate overshooting.

   *Required reading: Pugel, Chapter 19.*

14. **Government policies towards the foreign exchange (Apr. 21)**

   Defending a fixed exchange rate.
   Market interventions by the central bank.
Exchange controls.
Some historical experience: Gold Standard, Bretton Woods and recent days.

*Required reading:* Pugel, Chapter 20.
Practice Questions and Problems: 1-12

15. **Trade in capital and financial crises (Apr. 28)**

Gains and losses from international lending.
Lending to developing countries.
Financial crisis and their causes.
Resolving financial crisis and preventing them.

*Required reading:* Pugel, Chapter 21.
Practice Questions and Problems: 1-10.

16. **Final exam covering only Part III only (TBA)**