

Chapter One

International Economics Is Different

Nations are not like regions or families. They are sovereign, meaning that no central court can enforce its will on them with a global police force. Being sovereign, nations can put all sorts of barriers between their residents and the outside world. A region or family must deal with the political reality that others within the same nation can out-vote it and can therefore coerce it or tax it. A family or region has to compromise with others who have political voice. A nation feels less pressure to compromise and often ignores the interests of foreigners. A nation uses policy tools that are seldom available to a region and never available to a family. A nation can have its own currency, its own barriers to trading with foreigners, its own government taxing and spending, and its own laws of citizenship and residence.

As long as countries exist, international economics will be a body of analysis distinct from the rest of economics. The special nature of international economics makes it fascinating and sometimes difficult. Let's look at four controversial developments that frame the scope of this book.

FOUR CONTROVERSIES

Outsourcing

International outsourcing leapt to prominence in the early 2000s, when we noticed that firms in the United States and other industrialized countries were shifting service activities and jobs to developing countries, especially India. For a typical firm international outsourcing (or, as it is sometimes more suitably called, offshoring) can reduce its cost of these service activities by about half.

Why this outsourcing has received so much attention is part of what makes international economics different. Firms are always attempting to lower the costs that they incur in their production activities. If this occurs within the country, it is just part of everyday business decisions, with outsourcing being the “buy” part of the make-or-buy problem—how a firm sources the various materials, components, and services that it needs to carry out its overall production. But if the outsourcing crosses national boundaries, it can become a controversial political issue. What's new here is that international competition from developing countries is directly affecting white-collar workers in service activities that had previously been largely insulated.

(Interestingly, lost in much of the U.S. discussion is the fact that the United States overall is a large net *exporter* of business services [exports exceed imports]. U.S. firms actually gain much business through “inshoring” of work in such areas as computer, consulting, research, architectural, industrial engineering, and legal services.)

The start of the international outsourcing story is in India, which until 1991 had been following a policy aimed at self-sufficiency and government direction of the economy, with poor results. In 1991 the Indian government enacted a set of major liberalizations, including opening its economy to international trade and foreign companies. In the 1990s a number of U.S. and British companies quietly began to shift some back-office work like payroll processing to India, to take advantage of the availability of low-cost but educated workers who could speak English. Other firms, including Indian firms like Wipro and Infosys, noticed how successful this was, and began to expand the business further. At the same time the cost of voice and data transmission plummeted (a cost decline of more than 80 percent since 2000), with a rapid increase in the bandwidth in place between India and the United States and Britain.

This international outsourcing includes a range of business services, including data entry, telephone call centers, and software development. Firms in the United States and Britain are the largest users of international outsourcing. In addition to India, the Philippines, China, Russia, and the countries of Central Europe are also important providers.

How large is this international outsourcing? It seems to be rather surprisingly small for all the attention that it has received, though it is growing. A reasonable estimate is that by 2005 perhaps 600,000 service jobs (in total, not per year) had been shifted from the United States to India and other developing countries, a number which is less than one percent of service sector jobs in the United States. Another way to gain perspective on this number is to compare it to the flow of job gains and losses in the U.S. economy. *Each year* about 30 *million* people lose or quit their jobs (and something more than 30 million new jobs are filled).

Which kinds of jobs have been affected, or might be affected in the future? The work that is being outsourced is generally work that is repetitive and routinized. In the United States outsourcing seems to be a driver behind the decline in the number of lower-paid and somewhat less-skilled positions such as data entry keyers, phone operators in call centers, and computer programmers. Even though there is some outsourcing of higher paid and more skilled positions in the computer services area, the number of U.S. workers in such positions as computer software engineers has increased since the late 1990s, and their wages have risen faster than the economy average.

More generally, there is a limited range of service jobs that can be outsourced, because positions that require substantial face-to-face contact with customers or in-depth local knowledge cannot readily be outsourced. Essentially, the work that is most readily offshored is work that can flow internationally over wires. In total it appears that in the range of 11–18 percent of service sector jobs are *potentially* affected by international outsourcing, and most likely the actual number that will be offshored will be much less than this.

So, we have a new form of international trade, and white-collar workers, especially those in the information technology sector, feel threatened. Another thing that

is different about international economics is that national government officials have the power to enact laws and regulations that can limit international transactions. If the whole world were one country, the issue of outsourcing would be left to the marketplace. Within a country, it is usually impermissible for one region to restrict commerce with another region.

But the world is actually split into different countries, each with national policies. In the United States some politicians say that it is right and necessary to defend the jobs of American workers against the unfair outsourcing of those jobs to foreigners. If the product in question were a physical good, a possible defense would be obvious—some kind of a tax or other restriction on imports of the good into the country. This is the approach that President Bush used in 2002 when he imposed tariffs (a form of taxes) of up to 30 percent on steel imports into the United States. (Facing growing objections from steel-using firms and a ruling that the U.S. actions violated the rules of the World Trade Organization, he rescinded the tariffs in late 2003.)

In the case of international outsourcing of service sector activities and jobs, it's less clear what the government could do, because the products are intangible. One possibility would be a prohibition on shifting such work out of the country, but that would be draconian and probably difficult to enforce. Another narrower possibility would be to tilt government procurement rules, something that politicians do control, against outsourcing. We have seen a series of proposals at the state and federal levels to withhold or terminate government contracts with private firms if they offshore any of the work, but nearly all of these proposals have failed to pass.

Overall, the U.S. economy is very likely to benefit from international outsourcing of services, because it allows Americans to replace high-cost domestic production with lower-cost foreign provision of these services. This is the essence of comparative advantage as a basis for international trade and the gains from trading.¹ We will explore these aspects of international economics in Part I of this book. At the same time, we can feel compassion for the workers who lose their jobs in the process. One thing that U.S. politicians could do is to extend *trade adjustment assistance* (discussed in more depth in Chapter 10) to service workers who lose their jobs because of international outsourcing.

Immigration

About 200 million people, 3 percent of the world's population, live outside the country of their birth. For most industrialized countries (an exception is Japan), the percentage of the country's population that is foreign-born is rather high—13 percent for the United States and for Germany, 19 percent for Canada, 10 percent for Britain, and 23 percent for Australia—and rising. Many of the foreign born are illegal immigrants—about one-third of the total for the United States. The rising immigration has set off something of a backlash.

¹ Nobel Prize winner Paul Samuelson caused a stir when he pointed out in a 2004 article in the *Journal of Economic Perspectives* that it is possible for the United States to suffer a loss in well-being if the outsourcing that occurs leads to greater competition for U.S. exporters, so that the United States suffers a decline in its terms of trade. He did not offer any evidence that this was likely, but the general media implied that he just about said that it would happen. In Chapter 7 we examine why changes in the terms of trade are important to our understanding of economic growth.

In 2007 the U.S. Congress considered and rejected a bill to enact comprehensive reform of U.S. policies toward immigration. The bill, backed by President Bush and many Congressional leaders, would have shifted U.S. policy toward favoring new immigrants with more education and skills, created a new temporary guest worker program, increased requirements for employers to verify the legal status of their employees, built new fences along the U.S. border with Mexico and added new border guards, and created a complex process for illegal immigrants to gain legal status. After different groups in the United States raised their objections, including conservatives who focused on the latter provision and labeled it an unacceptable amnesty, support for the bill unraveled.

In the absence of federal changes, individual states have enacted hundreds of state laws about immigrants in recent years, many of them tightening up against illegal immigrants. For instance, Arizona voters in 2004 passed a proposition to stop government assistance to illegal immigrants (unless federal law explicitly requires it), and in 2006 they passed four more propositions to limit other benefits. Firms in Arizona can lose their right to operate if they employ illegal immigrants, and the sheriff of Phoenix has been aggressively arresting illegal immigrants.

Anti-immigrant rhetoric and actions have been rising in other countries. In France President Sarkozy took strong anti-immigrant positions and won election in 2007. Voters in Denmark, Switzerland, and Norway have shifted toward candidates who promise to reduce and restrict immigration. In Britain Prime Minister Brown unveiled the slogan “British jobs for British workers,” as part of an effort to show increased toughness on immigration. (Interestingly, Britain’s membership in the European Union poses immediate problems for Brown’s slogan. For citizens of other EU member countries, with the temporary exceptions of the newest members, Romania and Bulgaria, Britain is committed to allow free movement and the right to work.)

Opponents of immigration stress a range of problems that they believe arise from immigration, including general losses to the economy, the fiscal burden that may arise from immigrants’ use of government services (such as health care and schooling), slow integration of immigrants into the new national culture, values, and language, increased crime, and links of some immigrants to terrorism. What should one make of the claims of the opponents? Most immigrants move to obtain jobs at pay that is better than they can receive in their home countries, so it seems important to examine the economic effects.

How much harm do immigrants do to the economies of the countries they move to? International economic analysis helps us to think through the issue objectively, without being diverted by emotional traps. The answer is perhaps surprising, given the heat from immigration’s opponents.

As we will see in more depth in Chapter 15, such job-seeking immigration brings net economic benefits not only to the immigrants, but also to the receiving country overall. The basic analysis shows that there are winners and losers within the receiving country. The winners include the firms that employ the immigrants and the consumers who buy the products that the immigrants help to produce. The group that loses is the workers who compete with the immigrants for jobs. For instance, for the industrialized countries, the real wages of low-skilled workers have been depressed by the influx of low-skilled workers from developing countries. Putting all of this together, we find

that the net effect for the receiving country is positive—the winners win more than the losers lose.

It is important to recognize economic net benefits, but there will be fights over immigration as long as there are national borders. National governments have the ability to impose limits on immigration, and many do. If legal immigration is severely restricted by national policies, some immigrants move illegally. Migration, both legal and illegal, brings major gains in global economic well-being. But it remains socially and politically controversial.

China's Exchange Rate

An exchange rate is the value of a country's currency in terms of some other country's currency. Exchange rates are often sources of controversy, with conflict over the exchange-rate value of China's currency (the yuan, also called the renminbi) as the most intense in recent years.

In 1994 the Chinese government switched from a system of having several different exchange rates, each applying to different kinds of international transactions, to an unofficial but unmistakable fixed rate to the U.S. dollar. In fact, the exchange rate was locked at about 8.28 yuan per U.S. dollar from 1997 to 2005. During the Asian crisis of 1997–1998, the U. S. government praised the Chinese government's fixed exchange rate as a source of stability in an otherwise unstable region.

However, by 2003 the U.S. government began to complain that China's fixed rate policy was actually unacceptable currency manipulation. In 2004 the U.S. trade deficit (the amount by which imports exceed exports) with China was \$160 billion, a substantial part of the total U.S. trade deficit of \$612 billion with the entire world. These deficits were headed even higher in 2005, and the pressure from the U.S. government intensified. Bills introduced in the U.S. Congress threatened reprisals, including large new tariffs on imports from China, unless the Chinese government implemented a large increase in the exchange-rate value of the yuan. The European Union also had a large trade deficit with China, and it was also pressuring China to revalue the yuan.

Can keeping the exchange rate steady be manipulation? What this must mean is that the exchange rate value should have changed but did not. What was the evidence? The bottom-line evidence was that, especially after 2001, the Chinese government continually had to go into the foreign exchange market to buy dollars and to sell yuan, to keep the market rate equal to the fixed-rate target. If it had not done so, the strong private demand for yuan would have led to a rise in the price (the exchange-rate value) of the yuan. (Equivalently, the large private supply of dollars that were being sold to get yuan would have led to a decline in the value of the dollar against the yuan.)

There was evidence that the exchange-rate value of the Chinese currency was too low, but by how much? Various estimates of the degree of undervaluation were offered by economists, and most were in the range of 15 percent to 40 percent. Even for the experts, there are challenges in making this estimate.

First, while China had substantial trade surpluses with the United States and the European Union, it had trade deficits with many other countries, including South Korea, Thailand, the Philippines, Australia, Russia, Japan, and Brazil. Overall China had a trade surplus. It was not that large in 2004, though it was increasing.

Second, China has a remarkably high national saving rate. For a typical developing country, its low saving rate usually leads to a trade deficit, but China is not typical. So there is some economic sense for China to have a trade surplus.

Third, as the official pressure built on the Chinese government to change the exchange rate, private speculators began to move “hot money” into the country in the hopes of profiting when the value of the yuan increased. A substantial part of the government’s purchase of dollars was buying this hot money, and the hot money flow will reverse once the speculators think that the play is done.

For a few years, the Chinese government resisted the foreign pressure to change its exchange rate policy. The fixed exchange rate to the U.S. dollar had served the Chinese economy well. The Chinese government did not want to appear to be giving in to the foreign pressure, and it stated repeatedly that it alone would make any decisions about its exchange rate policy as it saw fit for the good of China’s economy.

Then, on July 21, 2005, the Chinese government announced and implemented changes in its policy toward the exchange-rate value of the yuan. It increased the value from 8.28 yuan per U.S. dollar to 8.11 yuan per dollar, a revaluation of 2.1 percent. (Yes, that does look odd, but the lower number means a higher value for the yuan. Welcome to the sometimes confusing world of foreign exchange. As stated, the numbers show a decrease in the value of a dollar, which is the same as an increase in the value of the yuan.) Thereafter, the Chinese government followed a policy best described as a “crawling peg,” in which the government allows small daily changes that result in a slow, tightly controlled change over time in the exchange-rate value. During the rest of 2005 the yuan value increased by only an additional 0.5 percent, during 2006 by 3.3 percent, and during 2007 by 6.5 percent. The rate of appreciation increased again during early 2008, so by mid-April 2008 the yuan had increased by a total of 15.4 percent, to a value of about 7 yuan per dollar.

However, the effects of the slow appreciation were overwhelmed by other trends. China’s trade surplus continued to increase, from \$49 billion in 2004 to \$309 billion in 2007. Foreign investments continued to flow into China. And China’s government had to continue to intervene to prevent the yuan from rising even more quickly, so that China continued to buy U.S. dollars in the foreign exchange market. China added the dollars to its holdings of official international reserve assets. These government holdings of foreign-currency denominated financial investments and similar assets had been \$170 billion at the beginning of 2001 and grew to \$719 billion by mid-2005. China’s international reserve holdings reached \$1 trillion in late 2006 and a staggering \$1.5 trillion in late 2007.

The United States and the European Union have continued to pressure China for a much larger increase in the exchange-rate value of the yuan. And China allowed a somewhat faster rate of increase. While the foreign pressure may have had some effect, the most important reason that China’s government allowed faster appreciation was that conditions in China’s national economy had changed. As the government intervened in the foreign exchange market to buy dollars, it was also selling yuan. The yuan money supply in China grew too rapidly, encouraging local borrowing and spending that created upward pressure on the inflation rate in China. Given these conditions, the increase in the exchange rate value of the yuan can assist the Chinese government to manage its domestic economy better, through at least three

channels. First, it lowers import prices in China, thereby reducing inflation pressures in China. Second, it slows the growth of China's exports, removing some of the demand pressure on the prices of resources and products. Third, it reduces the amount of intervention needed, reducing the pressure for growth of China's domestic money supply.

The international controversy over China's exchange rate was very much alive in mid-2008, and more will have happened since then. As the conflict over China's exchange rate policy shows clearly, policy decisions by one country have effects that spill over onto other countries. The exchange rate is a key price that affects international trade flows of goods and services and international financial flows.

In Parts III and IV of this book, we will examine in depth many of the issues raised in the description of this controversial situation. For example, in Chapter 16 we will examine trade surpluses and trade deficits in the context of a country's balance of payments. In Chapter 18 we will explore foreign financial investments and the role of currency speculation. In Chapters 22–24 we will examine how exchange rates and official intervention in the foreign exchange market affect not only a country's trade balance but also its national production, unemployment, and inflation rate. And in Chapters 20 and 25 we will look at why a country would or would not choose to have a fixed exchange rate.

Sovereign Wealth Funds

In 2007 sovereign wealth funds rose to prominence in discussions of the international financial system. Sovereign wealth funds are vehicles for national governments to seek high returns by investing in a full range of international financial assets, including the equity and debt of firms. As of late 2007 sovereign wealth funds had an estimated \$3 trillion in assets under management. Is this amount large or small? Sovereign wealth funds' assets are larger than the assets of hedge funds or private equity funds, but noticeably smaller than the assets of pension funds or mutual funds. The amount is equal to only about 2 percent of the value of all publicly traded debt and equity in the world. But, sovereign wealth funds are growing rapidly, with predictions that their assets will increase to \$10 trillion by the early 2010s.

Where does the government wealth to invest come from? One source is the foreign exchange intervention mentioned in the previous section about the Chinese yuan exchange rate. When a national monetary authority intervenes in the foreign exchange market to prevent the value of its currency from rising, it sells its currency and buys the target foreign currency, usually U.S. dollars. The dollars and other foreign currencies held by the national government are official international reserve assets that traditionally have been invested conservatively in U.S. government bonds or other low-risk, low-return debt securities. Because a national government holds these reserves for possible future use to intervene to prop up the value of its currency, it can make sense to hold the reserves in highly liquid if boring investments. But the low returns cost something—the country is earning little on this part of its national wealth. Countries with substantial reserve holdings can decide to use part of the holdings for more aggressive investments that earn higher returns. Singapore was the pioneer in this type of sovereign wealth fund. By late 2007, Singapore's Temasek Holding, set up in 1974, and its Government Investment Corporation, set up in 1981, had combined

assets estimated at nearly \$500 billion. China in 2007 used \$300 billion of its reserve holdings to form the China Investment Corporation.

A second source of wealth for the funds is the government revenue earned on exports of natural resources, especially crude oil. Essentially, the national wealth of resources in the ground is converted into national financial wealth, with the investment funds intended to produce income even after the resources have been depleted. Sovereign wealth funds based on oil revenues have two-thirds of the assets of all such funds. The largest are the funds of Abu Dhabi (started in 1976, assets estimated to be \$875 billion in late 2007), Norway (started in 1996, assets \$380 billion), Saudi Arabia (various funds, assets totaling \$300 billion), and Kuwait (started in 1953, assets \$250 billion).

Why are sovereign wealth funds controversial? After all, if their activities were within a country, they would look a lot like pension funds for government employees. The funds simply serve the standard financial function of moving funds from those who currently are net savers to those who currently are net borrowers.

Sovereign wealth funds are contentious because they operate internationally and are owned and controlled by national governments. Most funds (Norway is an exception) reveal very little about their operations or their investment holdings. Because of the secrecy of most sovereign wealth funds, it is easy to be suspicious of their motives and activities. The government owners say that the funds are managed by commercial standards to seek high returns while controlling risk exposure. Even if this is true, a fund's activities still can be controversial. In 2006 Norway's fund concluded that banks in Iceland were overvalued, and it sold short some of the bonds issued by these banks. It expected to earn returns when the prices of the bonds declined as other investors came to the same conclusion. Iceland's government took offense and complained that a supposedly friendly foreign government was attacking its financial institutions.

In other situations a government could obtain useful information through diplomatic means and pass that information to its sovereign wealth fund. The fund's use of that information would look like insider trading. Or, a government could use pronouncements and actions to attempt to influence financial market prices to the benefit of its fund. Or, the government could give a foreign firm favored access to its own national market to boost the value of its fund's investment in that foreign firm.

Furthermore, a government may use its sovereign wealth fund to pursue objectives other than financial returns, including the exercise of financial power for political gain. For instance, a government could use its investment position to alter company strategies, or to gain access to technology, know-how, or natural resources. The fund also can become embroiled in local political issues, as was Singapore's Temasek in Thailand when it purchased the telecommunication firm owned by the family of the then-Prime Minister Thaksin.

On top of all of this, international financial investing is challenging (as we will discuss in Chapter 18 of the book). A sovereign wealth fund must evaluate both the investment itself and the currency in which the investment is made. There is substantial potential for loss. For instance, in May 2007 China invested \$3 billion in Blackstone, a private equity group. By early 2008 the value of its investment had declined by \$1 billion (a loss of one-third of the value, measured in dollars, the

currency of the investment). The loss was even larger if measured in China's own currency (because the dollar depreciated against the yuan during this time period).

ECONOMICS AND THE NATION-STATE

It should be clear from the four controversies described above that international economics is a special field of study because nations are sovereign. Each nation has its own government policies. For each nation, these policies are almost always designed to serve some group(s) inside that nation. Countries almost never care as much about the interests of foreigners as they do about national interests. Think of the debate about international outsourcing. How loudly have Americans spoken out to defend the Indian and other jobs and incomes that would be lost if U.S. jobs and incomes are protected? Conversely, in India, where imports are also often impeded, how much outcry does one hear about how these import barriers are limiting jobs and incomes in the United States or Thailand?

The fact that nations have their sovereignty and their separate policies and their separate self-interests means that *nobody is in charge of the whole world economy*. The global economy has no global government, benevolent or otherwise. It is true that there are international organizations that try to manage aspects of the global economy, particularly the World Trade Organization, the International Monetary Fund, the United Nations, and the World Bank. But each country has the option to ignore or defy these global institutions if it really wants to.

Among the most important policies that each country can manipulate separately are policies toward the international movement of productive resources (people and financial capital), policies toward government taxation and spending, and policies toward money and exchange rates.

Factor Mobility

In differentiating international from domestic economics, classical economists stressed the behavior of the factors of production. Labor, land, and capital were seen as mobile within a country, in the sense that these resources could be put to different productive uses within the country. For example, a country's land could be used to grow wheat or to raise dairy cattle or as the site for a factory. But, the classical economists believed, these resources were not mobile across national borders. Outside of war land does not move from one country to another. They also downplayed the ability of workers or capital to move from one country to another.

If true, this difference between intranational factor mobility and international factor immobility would have implications for many features of the global economy. For instance, the wages of French workers of a given training and skill would be more or less the same, regardless of which industry the workers happened to be part of. But this French wage level could be very different from the wage for comparable workers in Germany, Italy, Canada, or Australia. The same equality of return within a country, but differences internationally, was believed to be true for land and capital.

This distinction of the classical economists is partly valid today. Land is the least mobile factor internationally. Workers and capital do move internationally, in response

to opportunities for economic gain. Still, there appear to be differences of degree in mobility interregionally and internationally. People usually migrate within their own country more readily than they will emigrate abroad. This is true partly because identity of language, customs, and tradition is more likely to exist within a country than between countries. In addition, national governments impose greater limitations on international migration than they do on relocation within the country. Capital is also more mobile within than between countries. Even financial capital, which in many ways is free to move internationally, is subject to a “home bias” in which people prefer to invest within their own country. In our analysis of international trade in Part I and Part II of this book, we will generally presume that some key resource inputs (to production of the traded products) cannot easily move directly between countries. We then examine international resource mobility in Chapter 15, and examine aspects of international financial investments in Part III.

Different Fiscal Policies

For each sovereign country, its separate government has its own public spending, power to tax, and power to regulate. As a rule, differences in the spending, tax, and regulatory policies of different countries are more pronounced than differences between the policies of states, provinces, or prefectures in one country. In the international arena, differences in tax policies can cause large flows of funds and products that would not have existed without the tax discrepancies. Banks set up shop in the Bahamas, where their capital gains are less taxed and their books less scrutinized. Shipping firms register in Liberia or Panama, where registration costs little and where they are free from other countries’ requirements to use higher-cost national maritime workers. Furthermore, each country’s array of import tariffs and export subsidies and duties are part of its separate fiscal policy. We examine the microeconomic effects of policies toward international trade in Part II, and the macroeconomic effects of different fiscal policies in Part IV.

Different Moneys

To many economists, and especially to regular people, the principal difference between domestic and international trade and investment is that international transactions often involve the use of different moneys. That is very different from transactions within a country. You cannot issue your own money, nor can your family, nor can the state of Ohio.

The existence of separate moneys means that the value of one money relative to another can change. We could imagine otherwise. If a U.S. dollar were worth exactly 10 Swedish kronor for 10 centuries, people would certainly come to think of a krona and a dime as the same money. But this does not happen. Since the 1970s the price ratios between the major currencies have been fluctuating by the minute. We must treat the dollar and the krona, for example, as different moneys. And, the exchange rate values can be contentious, as we saw for China’s yuan.

Most countries have their own national money, (though some countries share the same money). The supply of each kind of money is controlled by the monetary authority or central bank in charge of that money. Monetary policy affects not only the country using that money but also other countries, even if they use different moneys. Parts III and IV explore the special relationships between national moneys.

THE SCHEME OF THIS BOOK

International economics is exciting because there are differences between countries, and because these differences are important and sometimes controversial. While international economics is different, it is still like other economics in that we will be examining the fundamental challenge of scarcity of resources—how we can best use our scarce resources to create the most value and the most benefits. We will be able to draw on many standard tools and concepts of economics, such as supply and demand analysis, and extend their use to the international arena.

We begin our exploration of international economics with international trade theory and policy. In Part I we look at why countries trade goods and services. In Part II we examine what government policies toward trade would bring benefits and to whom. These first two parts of the book might be called international microeconomics. The focus of Parts III and IV shifts to finance and macroeconomics. In Part III we enter the world of different moneys, exchange rates, foreign exchange markets, balance of payments, and international investors. Part IV surveys the effects of a national government's choice of exchange rate policy on the country's macroeconomic performance, especially unemployment and inflation. In a few places this organization creates some momentary inconvenience, as when we look at the exchange rate link between cutting imports and reducing exports in Part I before we have discussed exchange rates in depth. Mostly the organization serves us well. The understanding we gain about earlier topics provides us with building blocks that allow us to explore broader issues later in the book.