

Announcements

- Midterm 2, Mon Nov 11th, 6:30-7:30
 - Location Blegen 5
 - Bring: **Ruler**, pencils, University ID
 - Q & A sessions this week
 - Wed Nov 6 (Hanson 1-104): 4-5:30pm, 7:30-9pm
 - Thurs Nov 7 (Anderson 270): 3:30-5:00pm
 - Extra Office hour Thursday 9-10 am (and your TA has office hours too)
 - Coverage: Lec6(i) though Lec10(ii)
 - Sample midterms already posted, with solution guides
 - 3 worksheets at moodle (weeks 6, 9, & 10)
 - 3 Readings on moodle

Real life example of industry that meet requirements of LR model

- Last class: We worked out **Long Run Industry Supply** for an industry with satisfying the following assumptions:
- Same Technology is available for all
- No barriers to entry
- Input prices to industry do not go up as the industry expands

Clear example: garden statue business



Real life example of industry that meet requirements of LR model

- Technology for making garden gnomes available for all.
- No restrictions to entry.
- It is such a small part of the market for all of its inputs (e.g. cement, paint, unskilled labor), that demand for garden gnomes could increase by a factor of 10 and it won't make any difference for the price of the inputs.

We concluded from last class:

- Long-run supply is **perfectly elastic** at $P = \text{MinATC}$
- In the short run, number of firms are fixed, but **in the long run firms can enter and exit freely**
- Firms will enter as long as there is economic profit. This causes price of the good to fall and eventually every single firm is breaking even

Broader Applications: elasticity

(of perfectly elastic LR supply)

As we just explained perfectly elastic LR supply makes sense for **garden gnome industry**. **Is the theory applicable for anything else?:**

Again the **Assumptions:**

- Same Technology is available for all
- No barriers to entry
- Input prices to industry do not go up as the industry expands

Other examples where model of perfectly elastic long-run supply is a sensible approximation?

How about week long ocean cruises? **(barriers to entry)**

- In the short run # vessels fixed (and captains), so in short run as demand goes up price of cruise increases
- In the long-run, we get more entry (and captains)

Should work for goods like:

- chicken
- granite countertops

Should work for gasoline market for a small country like Norway – **YES**
(input prices!)

But why won't the theory work as well for the gasoline market in the U.S.? (Hint U.S. consumes a large share of world oil supply)

Assumption 2: input prices

- If the US doubles its consumption of gasoline, this will drive up the price of oil (an input of gasoline, since the US has such a huge share of world demand). This causes the ATC curve to shift up.

Assumption 1: barriers to entry

What about the market for playing 18 holes of golf in...

Manhattan?

Anywhere in North Dakota?

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What about the market for playing 18 holes of golf in...

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We expect the price of golf to go up in Manhattan as space constraints keeps more firms from entering. The price of golf will remain high in the long run.

Anywhere in North Dakota?

In North Dakota, there is enough space to expand, so our framework of firms will probably work better since firms can enter and exit more freely.

Assumption 1: barriers to entry

What about the market for playing 18 holes of golf in...

Manhattan?

NO

We expect the price of golf to go up in Manhattan as space constraints keeps more firms from entering. The price of golf will remain high in the long run.

Anywhere in North Dakota?

YES

In North Dakota, there is enough space to expand, so our framework of firms will probably work better since firms can enter and exit more freely.

Application 1: Imports (class ex)

Impact of Imports

Initial Situation: No imports from China.

(Because not developed enough or because of import restrictions)

New Situation:

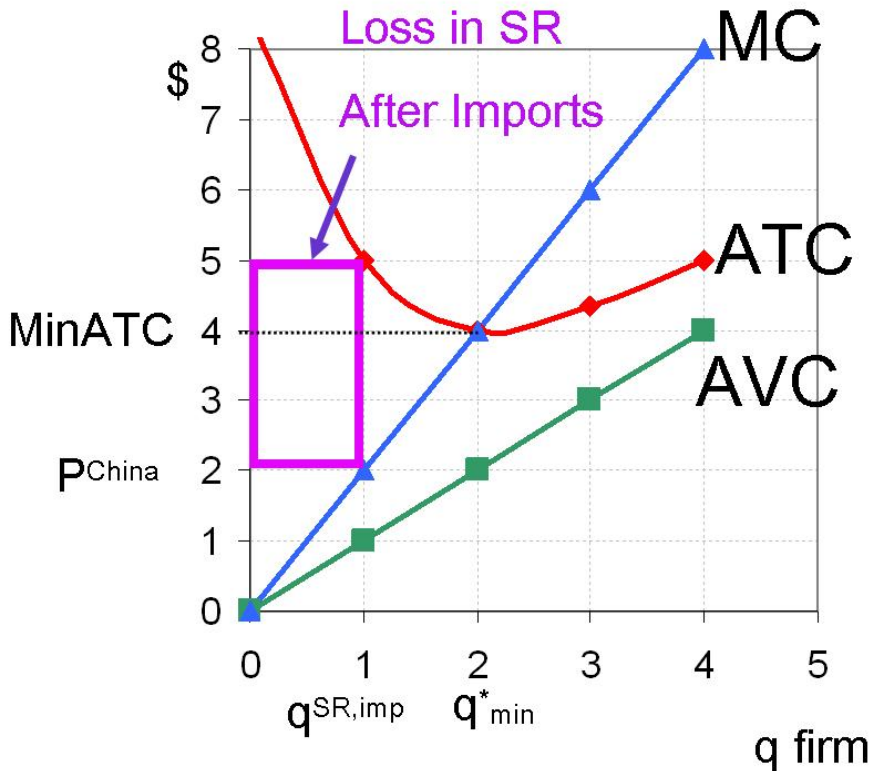
Imports come in from China at price $P^{\text{china}} = 2$

Distinguish between short and long run, we want to know the equilibrium once we are importing, both in the short run and in the long run.

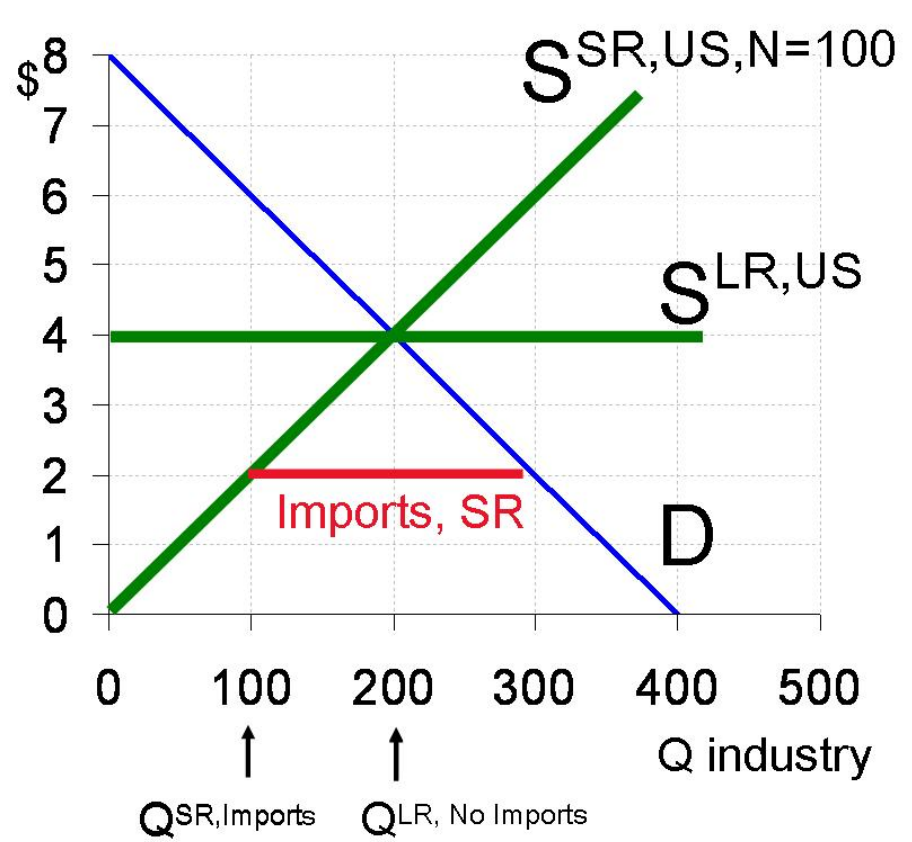
Lets calculate: P , Q , q , N , imports.... (on whiteboard)

Impact of Imports in the Short and Long Run

Suppose the following cost structure and demand:



Cost Structure of Firms



Industry Level Variables

Application2 Imports (reading 6)

So we see that the domestic production in the last slide is completely shut down.

How about in the real world? It's less extreme.

Let's take a look at a list of industries hit by a surge from China

Reading 6

- International Application

Consumer Goods Manufacturing:

The Rise of China and Plant Exit in the United States

	Import Share of Shipments (percent)		China Share of Imports (percent)		Percent Change in U.S Employment 1997-2007
	1997	2007	1997	2007	
Industry					
Curtain & drapery mills	8	56	38	65	-47
Other household textile prod mill	22	68	25	49	-51
Women's & girls' cut & sew dress	29	67	21	55	-71
Women's & girls' cut & sew suit,	48	92	19	49	-91
Infants' cut & sew apparel mfg	60	99	8	62	-97
Hat, cap, & millinery mfg	44	80	26	67	-74
Glove & mitten mfg	58	88	50	63	-78
Men's & boys' neckwear mfg	25	56	2	59	-67
Other apparel accessories	39	80	35	64	-75
Blankbook, looseleaf binder,	18	47	43	52	-51
Power-driven handtool mfg	28	56	18	46	-56
Electronic computer mfg	12	49	0	56	-68
Electric housewares & fan mfg	52	78	48	76	-54
Wood household furniture mfg	29	62	18	46	-51
Metal household furniture mfg	29	55	37	85	-48
Silverware & plated ware mfg	44	91	31	73	-82
Costume jewelry & novelty mfg	31	68	31	67	-63
Mean of China Surge Industries (N=17)	34	70	26	61	-66

Within industries, the segments that have survived tend to be different from the part that has left.

Example of **wood furniture industry**

- In 1997 and earlier, dominated by places like Highpoint, NC
- Large plants making **standardized products** for **mass market**.
- These places mostly in South
- Custom, hand crafted segment scattered around the country in small plants
 - Need to be close to supply of craftsman (e.g. Amish)
 - Good to be close to consumers for custom work

Example of clothing industry

- Also dominated by places in the South
- New York city retained fashion element in small craft-oriented plants

What has happened?

- China is knocking out the large plants in North Carolina making standardized goods for the mass market.(China: the new North Carolina)
- Small plants doing custom work have increased share (and places like New York)

China's comparative advantage is weakest in:

- 1) **Custom element** (helps to be close geographically for this, quicker turnaround, better communication)
- 2) Cases with **high end niche products**, with premium on fashion and creativity.

Even for these segments, the future does not look so great for American manufacturers

- 1) Small segment
- 2) communication getting better so possible to do custom at a distance.
- 3) China moving up **quality ladder**

Closer look at the remaining domestic producers

Toys

- 1600 employees left in “Doll and Stuffed Toy Manufacturing” in 97 establishments.
- One plant with over 500 employees in Burlington Vermont. What does this “factory” do?





- What about the little guys producing toys in the U.S.? An interesting article in NY Times cited in the Reading 6
- New safety laws requiring inspections (imposed because of lead paint used in some imported toys from China) are particularly burdensome on these small craft shops.
- Too small to enjoy economies of scale in inspections.





By way of comparison...



- But US still keeps some manufacturing...

