

Midterm Exam

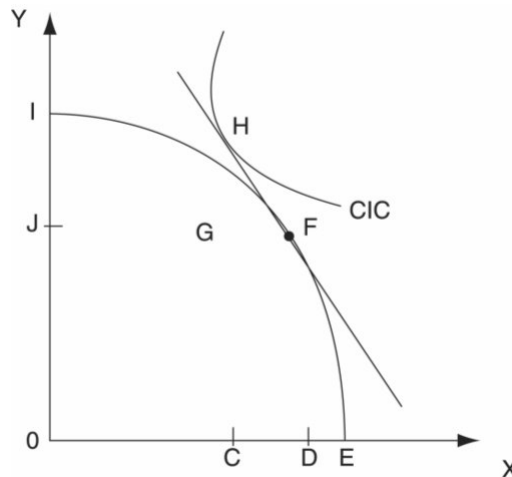
Name _____

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Instructions: There are two parts to this midterm. Part A consists of multiple choice questions. Please mark the answers to the multiple choice questions on the exam paper. Part A has 25 questions and is worth 60%. Part B is worth 40% and consists of short answer questions.

Part A: MULTIPLE CHOICE. Choose the one alternative that best completes the statement or answers the question.

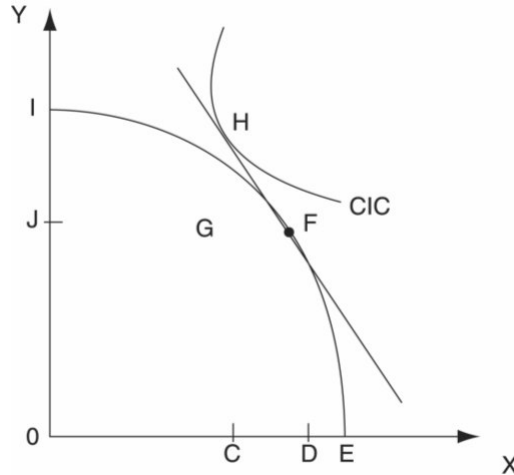
Answer the question(s) below based on the following diagram of a country that is in international trade equilibrium. Point G lies at the intersection of the straight lines between CH and JF. CIC represents the national indifference curves.



- 1) Refer to the figure above. If this country is labor abundant, then according to the HO theory good X should be _____ intensive. 1) _____
 - A) labor
 - B) capital
 - C) both capital and labor
 - D) Can't tell without more information

- 2) According to the HO model, 2) _____
 - A) the gainers from trade outnumber the losers from trade.
 - B) the scarce factor necessarily gains from trade.
 - C) everyone automatically gains from trade.
 - D) None of the above.

Answer the question(s) below based on the following diagram of a country that is in international trade equilibrium.



- 3) Refer to the figure above. This country has comparative advantage in 3) _____
 A) X. B) Y.
 C) both X and Y. D) Can't tell without more information.

Answer the question(s) below based on the information in the following table, where the numbers represent the number of labor hours it will take to produce a unit of the given good

	Spain	France
Grapes	3	9
Textiles	1	2

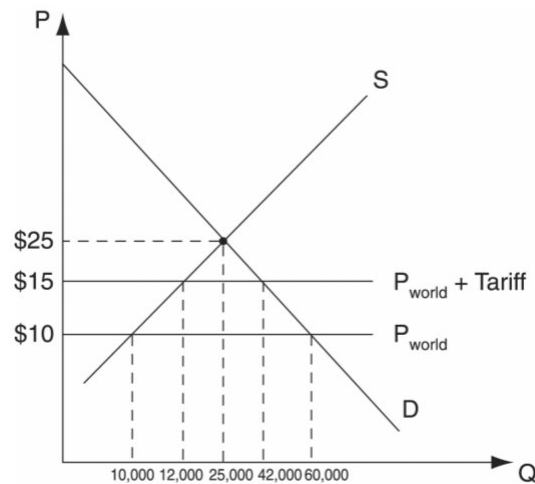
The numbers represent the number of labor hours it will take to produce a unit of the given good.

- 4) Refer to the table above. Once trade begins, a possible international price (i.e. terms of trade) for textiles in terms of grapes is 4) _____
 A) 4/15. B) 2. C) 2/5. D) \$5.
- 5) A production subsidy combined with free trade 5) _____
 A) has the same deadweight costs as a tariff.
 B) has only production deadweight costs.
 C) has only consumption deadweight costs.
- 6) The simultaneous export and import of widgets by the United States is an example of 6) _____
 A) increasing returns to scale.
 B) imperfect competition.
 C) intra-industry trade.
 D) inter-industry trade.
 E) None of the above.

- 7) If output more than doubles when all inputs are doubled, production is said to occur under conditions of _____
- A) increasing returns to scale.
 - B) imperfect competition.
 - C) intra-industry trade.
 - D) inter-industry trade.
 - E) None of the above.
- 8) If a tariff on bikes causes domestic bike prices to rise by 20% and domestic value added in the domestic bike industry to rise by 30%, then _____
- A) the effective rate of protection is higher than the nominal rate.
 - B) the effective rate of protection of bikes is 30%.
 - C) the nominal rate of protection of bikes is 20%.
 - D) All of the above.
- 9) Which of the following is true (assume the small country case)? _____
- A) With either a tariff or a quota, an increase in demand leads to a higher price and more imports.
 - B) With a tariff, an increase in demand leads to a higher price and more imports.
 - C) With a quota, an increase in demand leads to a higher price and more imports.
 - D) None of the above are true.
- 10) Comparative advantage is determined by _____
- A) actual differences in labor productivity between countries.
 - B) relative differences in labor productivity between countries.
 - C) Both A and B.
 - D) Neither A nor B.
- 11) Consider a scenario where monopolistic competition prevails. When there are economies of scale, an increase in the size of the market will _____
- A) increase the number of firms and lower the price per unit.
 - B) decrease the number of firms and lower the price per unit.
 - C) decrease the number of firms and raise the price per unit.
 - D) increase the number of firms and raise the price per unit.
 - E) None of the above.
- 12) In theory, countries can impose tariffs _____
- A) only on exports.
 - B) only on imports.
 - C) on both imports and exports.
 - D) on imports, exports, and nontraded goods.

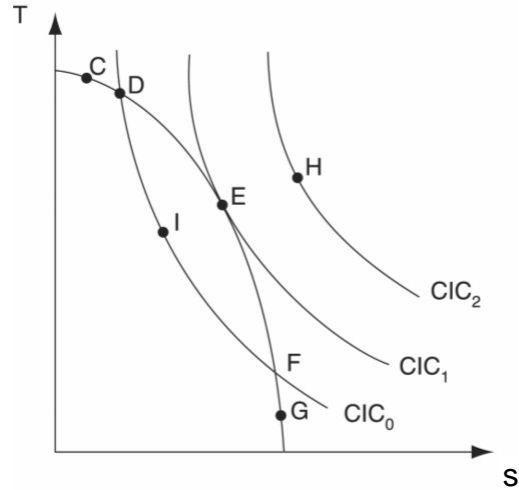
- 13) If the autarky price of S were lower in country A than in country B, then if trade were allowed 13) _____
 A) A would likely export S to B. B) A would likely import S from B.
 C) neither country would want to trade. D) None of the above.
- 14) In the HO model, the production possibility frontier is bowed out due to the assumption of 14) _____
 A) increasing returns to scale.
 B) identical tastes.
 C) different factor intensities in the production of the two goods.
 D) Two of the above.
- 15) Let K_j and L_j denote the capital and labor inputs in the production of good j ($j=S,T$), then S is said 15) _____
 to be capital intensive relative to T if
 A) $L_S < L_T$. B) $K_S/L_S > K_T/L_T$.
 C) $K_S > K_T$. D) All of the above.
- 16) According to the factor price equalization theorem, if A is labor abundant, then once trade opens 16) _____
 A) wages should rise and rents should fall in A.
 B) wages and rents should fall in A.
 C) wages should fall and rents should rise in A.
 D) wages and rents should rise in A.

Answer the question(s) below based upon the following diagram.



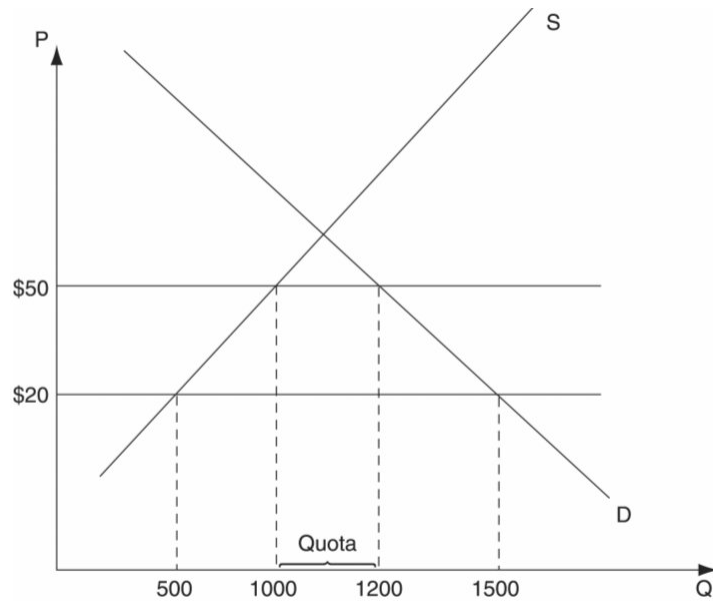
- 17) Refer to the figure above. Domestic producers gain _____ because of the tariff. 17) _____
 A) \$150,000 B) \$15 C) \$120,000 D) \$55,000

Answer the question(s) below based on the following diagram.



- 18) Refer to the figure above. Which of the following is true? 18) _____
- A) A move from C to D would raise community satisfaction.
 - B) The relative price of T is higher at C than at F.
 - C) The relative price of S is higher at G than at D.
 - D) All of the above are true.
- 19) If Canada imposes a tariff on bananas and if none are grown in Canada, this tariff has 19) _____
- A) only revenue effects.
 - B) only protective effects.
 - C) both protective and revenue effects.
 - D) neither protective nor revenue effects.

Answer the question(s) below based on the following diagram.



- 20) Refer to the figure above. If the government was to auction quota licenses competitively, it could earn up to _____ 20) _____
 A) \$5000. B) \$2000. C) \$10000. D) \$6000.
- 21) In autarky equilibrium, _____ 21) _____
 A) exports equal imports. B) there is no trade.
 C) production equals consumption. D) All of the above.
- 22) Internal economies of scale arise when the cost per unit _____ 22) _____
 A) rises as the industry grows larger.
 B) falls as the industry grows larger.
 C) rises as the average firm grows larger.
 D) falls as the average firm grows larger.
 E) None of the above.

Answer the question(s) below based on the information in the following table

	Country	
Goods	A	B
Beer	3	9
Wine	1	2

(numbers indicate hours of labor per unit of output)

- 23) Refer to the table above. For trade to occur along the lines of comparative advantage, wages in A relative to wages in B (measured in the same currency) 23) _____
- A) must be greater than \$2 but less than \$3.
 - B) must be at least twice but less than 3 times as great.
 - C) must be less than three times as small.
 - D) Need more information to answer.
- 24) Refer to the table above. Country A has a comparative advantage in 24) _____
- A) beer.
 - B) wine.
 - C) both beer and wine.
 - D) neither beer nor wine.
- 25) Which of the following is true? 25) _____
- A) In the Ricardian model, complete specialization seldom occurs due to the assumption of increasing opportunity costs.
 - B) Complete specialization is more likely if opportunity costs change little as the production point moves closer to either axis.
 - C) In the HO model complete specialization in the production of exports is a likely outcome of international trade.
 - D) All of the above are true.

Part B: SHORT ANSWER QUESTIONS (40%)

Please answer the following short answer questions. **For essay type questions, please keep your answers for each question to a length of one page.** Points are awarded for the succinctness, consistency and clarity of your answer. **You will not get points for verbosity.** Feel free to use graphs (as they apply) to help elucidate your answer. Show any calculations as necessary in answering the questions.

26. (10%) This question is an application of what you learnt and saw in classes. Suppose that the world consists of two countries only, A and B. Use general equilibrium diagrams for both countries to show the effect on each country of country A imposing a tariff on its imports.

27. (10%) Within the Heckscher-Ohlin framework, assume that the two industries are automobiles and wheat. The automobiles industry is assumed to be capital intensive and the wheat industry, labor intensive. Suppose you are in the capital abundant country.

(i) [3 pts] Using the diagram below, draw a candidate free trade equilibrium for the country.



(ii) [3 pts] In the diagram above, show what happens if the price of automobiles rise.

(iii) [4 pts] Suppose that you are a laborer in the wheat industry. As a result of the price increase in the automobile industry, are you better off or worse off? Explain!

28. (20%) If you were an import-competing producer in a growing domestic market (i.e. demand shifting out), which trade instrument would you prefer in terms of its ability to protect you from foreign competition – a tariff, an import quota, or a subsidy? Please explain. [Note: credit is only given for your explanation!]