

NAME: _____

Student ID No.: _____

**Economics 340
International Economics
Prof. Alan Deardorff
First Midterm Exam**

Form 0

Answers

February 19, 2018

INSTRUCTIONS: READ CAREFULLY!!!

1. Please do not open the exam until you are told to do so.
2. **PLACE YOUR NAME AND STUDENT ID NO. (THE EIGHT DIGIT NUMBER FROM YOUR M-CARD) ON THE EXAM AND ON THE SCANTRON SHEET.**
3. Find the **FORM NUMBER** above and enter it where it asks for “KEY” on the scantron sheet. Be sure to fill in the bubbles.
4. This exam has 100 points and you have approximately 80 minutes to complete the test. Check that you have all ?? pages of the exam, including this cover sheet.
5. **Part 1** consists of 25 multiple choice questions worth 2 points each. Answers to the multiple-choice questions in Part 1 should be marked on the scantron sheet using a #2 pencil. There are no penalties for guessing.
6. **Part 2** consists of short-answer questions for which you must provide written answers on these sheets. Point values for questions in Part 2 are indicated in parentheses. Part 2 has 48 points total.
7. That leaves 2 points unaccounted for. You will get these if (and only if) you put your name and ID number on both this exam booklet and the scantron sheet, **and** if you enter the form number (see above) on the scantron.
8. Good luck!

FORM 0

Economics 340 First Midterm Exam

Part 1: Multiple Choice (2 points each; 50 points total)

Select the **best** answer of those given. Answers to this part should be marked on the scantron sheet using a #2 pencil. There is only one correct answer per question, and there is no penalty for guessing.

1. Where does the largest share of Michigan's imports come from?
 - a. Canada
 - b. China
 - c. Mexico
 - d. European Union
 - e. Japan

Ans: c

2. Which of the following has been called the "voice of developing countries"?
 - a. World Intellectual Property Organization
 - b. United Nations Conference on Trade and Development
 - c. World Bank
 - d. Organization for Economic Cooperation and Development
 - e. International Monetary Fund

Ans: b

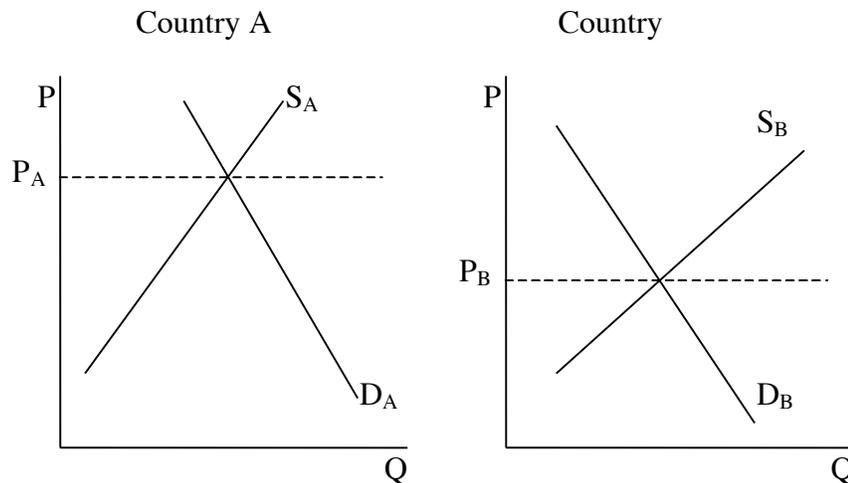
3. When the IMF was first created, one of its main functions was to
 - a. Assist countries in devaluing their currencies so as to stimulate employment.
 - b. Prevent countries from raising tariffs on imports as a means of stimulating employment.
 - c. Enforce the freedom of international capital flows.
 - d. Assure that exchange rates were freely flexible.
 - e. Assist countries in maintaining pegged exchange rates.

Ans: e

4. Which of the following was the name of one of the GATT negotiating rounds?
- NAFTA
 - Wilbur
 - Nixon
 - Seattle
 - Uruguay

Ans: e

5. The graphs below show domestic supply and demand curves for a good in two countries, with prices measured in the same currency. If these are the only two



countries in the world and if they open to free international trade,

- Demanders of the good in Country A will benefit from trade.
- Suppliers of the good in Country A will benefit from trade.
- The welfare of Country A as a whole will fall.
- The quantity of the good demanded in Country B will become larger.
- The price of the good in both countries will be the one labeled P_B .

Ans: a

6. Suppose that Austria and Belgium have the unit labor requirements for producing steel and brooms shown in the table at the right. Then

Unit labor	Country
------------	---------

- a. Belgium has a comparative advantage in brooms.
- b. Austria has a comparative advantage in steel.
- c. Austria has an absolute advantage in steel.
- d. Belgium has an absolute advantage in brooms.
- e. All of the above.

		Austria	Belgium
Good	Steel	3	4
	Brooms	6	1

Ans: e

7. For two countries, Angola and Belize, the top row of the table at the right shows the wages of labor, both expressed in U.S. dollars, when they are engaged in free international trade. Below that are shown the quantities of labor that each requires, in a Ricardian model, to produce one unit of each of two goods, chips and ducks. In this free-trade equilibrium, what is the U.S. dollar price that consumers in Angola pay for chips?

		Country	
		Angola	Belize
Wage		\$2	\$2.50
Unit labor req:			
Good	Chips	24	18
	Ducks	30	40

- a. \$36
- b. \$45
- c. \$48
- d. \$60
- e. \$100

Ans: b

8. According to the Heckscher-Ohlin model of international trade, countries have a comparative advantage in goods that
- a. Use relatively intensively their relatively abundant factors.
 - b. Display the strongest increasing returns to scale.
 - c. Use less labor, per unit of output, than is used to produce the same good in other countries.
 - d. Use less labor, per unit of output, than is used in the same country in other industries.
 - e. Have the most competition among the largest number of firms.

Ans: a

9. Factor Price Equalization means that,
- All workers are equally productive.
 - If a country fails to trade, its skilled workers will earn no more than its unskilled workers.
 - Trade causes the return to human capital to be the same as the return to physical capital.
 - For countries to trade fairly, they must tax factors of production so that firms in all countries pay the same factor prices.
 - Free trade causes identical factors in different countries to be paid more nearly the same than they would be in autarky.

Ans: e

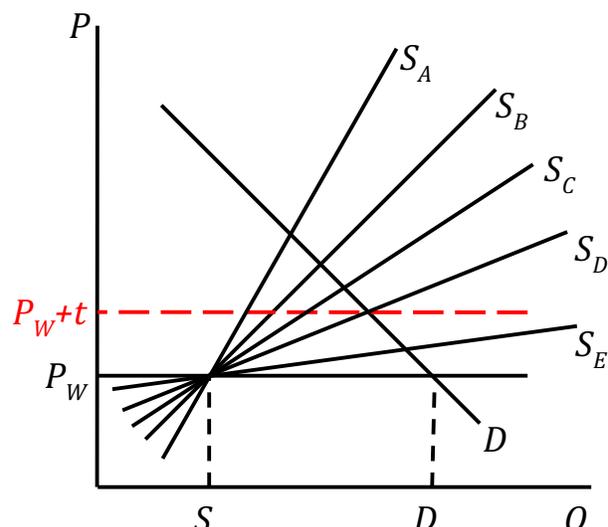
10. In the game between Boeing and Airbus described by Krugman, the subsidy paid to Airbus by its government causes
- Airbus to want to produce whether or not Boeing produces.
 - Boeing to cease production
 - Airbus and its government, combined, to benefit.
 - All of the above.
 - None of the above.

Ans: d

11. Suppose that Thailand is a small country that imports fudge, which it also produces itself under free trade. If Thailand levies a tariff on imports of fudge, then

- The price of fudge on the world market will fall.
- The price of fudge in Thailand will fall.
- Consumers in Thailand will buy a larger total quantity of fudge.
- Consumers in Thailand will buy more fudge from producers in Thailand.
- Fudge producers in Thailand will have to pay the tariff.

Ans: d



12. In the graph, initial price is P_W and quantities are S_0 and D_0 . A tariff, t , is then applied to imports. For which of the supply curves is the dead-weight loss from the tariff largest?
- a. S_A
 - b. S_B
 - c. S_C
 - d. S_D
 - e. S_E

Ans: d

13. A specific tariff is
- a. An import tax that must be paid in kind (i.e., giving the government the good itself).
 - b. Any tax on a particular imported good (as opposed to one on all imports).
 - c. A requirement to pay the government a specified fraction of the monetary value of an imported good.
 - d. A tax on imports defined as an amount of currency per unit of the good.
 - e. The revenue that the government earns by auctioning off import quotas.

Ans: d

14. When the United States imposed a VER on cars from Japan
- a. Japanese firms received the rents from the quantitative restriction.
 - b. Japanese car companies responded by lowering the U.S. prices of their cars.
 - c. Japanese car companies responded by lowering the quality of the cars they sold in the U.S.
 - d. The effect was to restrict U.S. car imports from all foreign countries.
 - e. The VER was implemented by the U.S. levying a 25% tariff on cars from Japan.

Ans: a

15. The European Union has a “variable levy” on imports of butter. This means that when the world price of butter goes up,
- a. The EU must have increased its tariff on butter.
 - b. Consumers of butter in the EU benefit.
 - c. The EU reduces the size of the tariff that it levies on butter.
 - d. The EU tariff on butter goes up with it.
 - e. Cows in the EU get angry.

Ans: c

16. If one country pays a subsidy to its producers of a product,
- a. Foreign producers gain.
 - b. Foreign consumers lose.
 - c. Foreign countries that are net importers of the product lose.
 - d. Foreign countries that are net exporters of the product lose.
 - e. All of the above.

Ans: d

17. When U.S. industries claim that imports are “unfair,” that claim is evaluated by
- a. The International Trade Commission
 - b. An agency that is part of the Commerce Department
 - c. The U.S. Department of International Trade and Industry
 - d. The Ways and Means Committee of the U.S. House of Representatives
 - e. USTR

Ans: b

18. Trade Adjustment Assistance

- a. Includes extended unemployment compensation for workers laid off due to increased imports.
- b. Is money given by the WTO to developing countries to help them implement their obligations as members.
- c. Includes assistance provided by the World Bank to countries seeking to subsidize their exports.
- d. Is a permanent subsidy given by the U.S. government to firms so that they can avoid closing down in the face of import competition.
- e. Is a popular form of industrial policy, designed to help strong firms become even more competitive on world markets.

Ans: a

19. What country prevented the formation of the International Trade Organization?

- a. India
- b. Russia
- c. The United Kingdom
- d. The United States
- e. None. The ITO is another name for the World Trade Organization.

Ans: d

20. A country's "bound tariff" on a good is

- a. The tariff that it intends to levy after it escapes from poverty.
- b. The maximum that it may normally charge without violating its GATT commitments.
- c. The tariff level imposed on it by its partners in a preferential trade agreement.
- d. The highest tariff it can charge without driving imports to zero.
- e. 100%.

Ans: b

21. Which of the following is **not** one of the WTO's permitted exceptions to the MFN requirement?

- a. Anti-dumping duties
- b. Countervailing duties
- c. GSP
- d. VERs
- e. Free trade areas

Ans: d

22. In the assigned reading by Borjas on immigration, the author argues that, compared to earlier waves of immigrants to the US, recent immigrants

- a. Will assimilate more slowly because of religious differences.
- b. Will assimilate more rapidly because of their higher incomes and levels of education.
- c. Will assimilate more slowly because their countries of origin are further away.
- d. Will assimilate more rapidly because the US population is more welcoming.
- e. Will assimilate more slowly because they are less diverse ethnically.

Ans: e

23. The NAFTA was expected to reduce migration from Mexico into the United States because

- a. The NAFTA agreement included a provision for increased enforcement of migration restrictions at the border.
- b. The NAFTA would reduce the movement of vehicles across the border in which illegal migrants could hide.
- c. The NAFTA was expected to raise wages in Mexico, reducing the incentive for migration.
- d. The NAFTA was expected to reduce American wages below Mexican wages, causing migration to flow into Mexico instead of into the U.S.
- e. The NAFTA would improve the air quality in Mexico, so that Mexicans would not want to leave.

Ans: c

24. Did the United States, in recent weeks, collect a tariff on imports of airplanes from Canada's Bombardier company? Why, or why not?
- a. Yes, because their price was unfairly low
 - b. No, because the USITC said that the planes did not cause injury
 - c. Yes, because President Trump wanted to improve the US trade balance
 - d. No, because the International Trade Administration said they were not being dumped
 - e. Yes, because Bombardier was conspiring with the European company, Airbus

Ans: *b*

25. Why did President Trump travel to Davos?

- a. To relax at a hotel he owns
- b. To ski
- c. To give a speech at the European Parliament
- d. To attend the World Economic Forum
- e. He didn't. The invitation was revoked.

Ans: *d*

Part II: Short Answer (points indicated; 48 points total)

Answer on these sheets in the space provided.

1. (6 points) What do the following acronyms stand for in international economics?

- a. GATT *Ans: General Agreement on Tariffs and Trade*
- b. ILO *Ans: International Labor Organization (or Office)*
- c. NAFTA *Ans: North American Free Trade Agreement (or Area)*
- d. DWL *Ans: Dead-weight loss*
- e. VER *Ans: Voluntary Export Restraint*
- f. USTR *Ans: United States Trade Representative*

2. (3 points) True-False. Circle the correct answer.

- a. Rich country governments pay more in subsidies to their farmers than they pay in aid to poor countries. True False *True*
- b. Michigan's share of trade in GDP is larger than any other US state True False *True*
- c. The U.S. owns more assets abroad than foreigners own of assets in the U.S. True False *False*

3. (8 points) Each of the first three tables below shows the amounts of labor required to produce one unit of each of two goods, X and Y, in two countries, A and B. These are the only goods, and the only countries, in the world. In each case, fill in the blanks with “X,” “Y,” “A,” “B,” “both,” or “neither.”

a. Country A has absolute advantage in good	<u>neither</u>		Labor needed per unit of output		Country
Country B has comparative advantage in good	<u>X</u>		Good		A B
			X		20 10
			Y		40 32

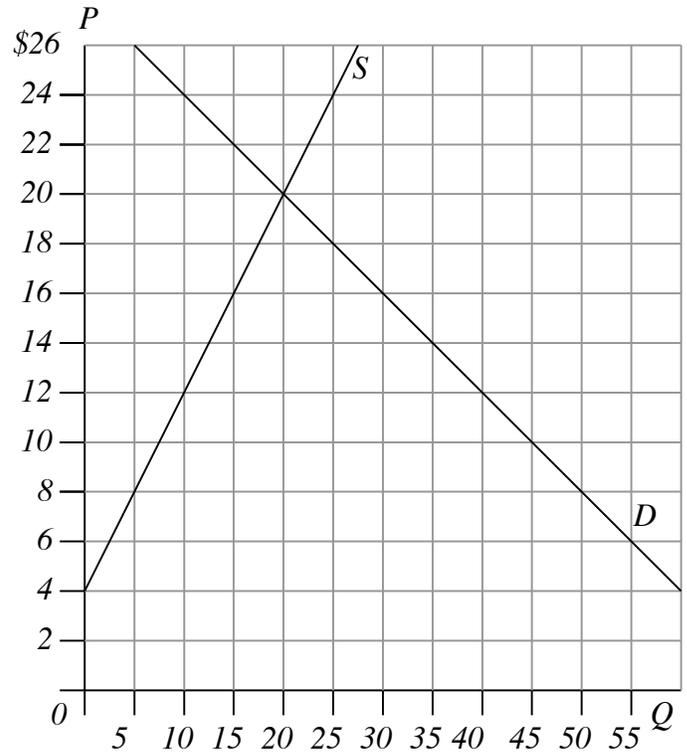
b. Country with absolute advantage in good X:	<u>A</u>		Labor needed per unit of output		Country
Country with comparative advantage in good Y:	<u>A</u>		Good		A B
			X		1040 1080
			Y		200 300

c. Country that exports good X:	<u>B</u>		Labor needed per unit of output		Country
Country that exports good Y:	<u>A</u>		Good		A B
			X		10 8
			Y		0.04 0.04

The table below looks much like the ones above, but this one gives a different kind of information: output per worker (i.e., productivity). Fill in the blanks as above.

d. Country that exports good X:	<u>B</u>		Output produced per unit of labor		Country
Country that exports good Y:	<u>A</u>		Good		A B
			X		120 100
			Y		9 6

6. (10 points) In the graph at the right, supply and demand curves are drawn on a grid from which you can read corresponding prices and quantities. The curves represent the domestic supply and demand for a good in a small country. Use them to answer the questions below in the blanks provided. Feel free to add whatever you need to the graph, but this will not count for or against your answers.



a. What is the autarky price?

_____ \$20 _____

b. Suppose that the world price were \$8. What would be the domestic price if trade were free?

_____ \$8 _____

c. At this world price of \$8, how much would the country demand of the good, how much would it supply, and how much would it import?

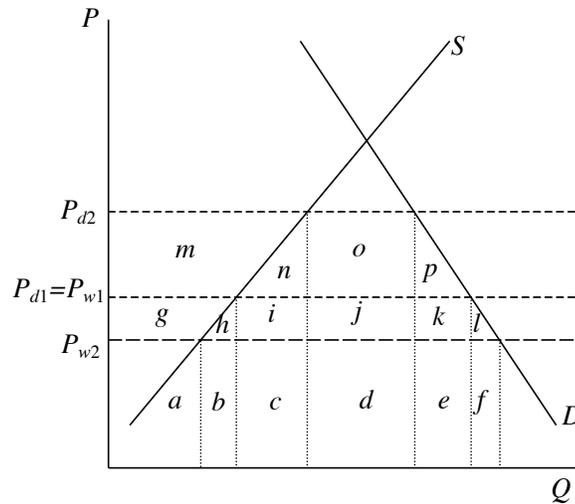
Demand = _____ 50 _____ Supply = _____ 5 _____ Imports = _____ 45 _____

d. Suppose now that trade is not free, and instead there is an import quota of 15 units of the good. What is now the domestic price, and how much does the country demand and supply? How much also is the quota rent?

Price = _____ \$16 _____ Demand = _____ 30 _____ Supply = _____ 15 _____ Rent = _____ \$120 _____

e. If the world price were now to rise from \$8 to \$22, with the quota still in place, how much of the good will be demanded on the domestic market?

Demand = _____ 15 _____



7. (6 points) The figure above shows domestic supply and demand for a good in a *large* country. Initially, with free trade, it faces the world price P_{w1} . It then levies a tariff, and this causes the world price to fall to P_{w2} while the domestic price rises to P_{d2} . Using the prices and areas labeled in the figure, answer the following.

a. What is the size of the tariff?

The tariff is the difference between the new domestic price and the new world price: $P_{d2} - P_{w2}$.

b. How much will domestic suppliers of this good gain or lose from the tariff?

Suppliers gain the change in producer surplus, which is: $+m$.

c. How much will domestic demanders of this good gain or lose from the tariff?

Demanders lose the change in consumer surplus, which is: $-(m+n+o+p)$.

d. How much does the government of the country collect in revenue from the tariff?

Government collects the tariff times the new quantity of imports, thus area: $+(o+j)$.

8. (6 points) Define the following terms as they are used in international economics:

- a. Stolper-Samuelson Theorem *Ans: The implication of the Heckscher-Ohlin model that scarce factors lose from international trade and abundant factors gain.*
- b. Intra-industry trade *Ans: Export and import within the same industry.*
- c. Ad valorem tariff *Ans: A tax on imports defined as a percentage of the value of the good.*
- d. Countervailing duty law *Ans: A law that places a tariff on imports that are subsidized by a foreign government.*
- e. Most favored nation *Ans: The principle of the GATT and WTO that members should charge, on imports from all members, the lowest tariff that they charge against any member; i.e., it prohibits discrimination across imports from other members.*
- f. Brain drain *Ans: The migration out of a country of its most educated and skilled people.*