

ECON3171

Midterm #1 Review Topics and Questions

This document is intended to provide you with a brief recap of the topics that will be on the first midterm exam, Wednesday September 26, 2007. The test will be comprised of 50 multiple choice questions and answers will be given on scantron form XXXXX.

The exam is constructed so that you reveal your understanding of the material as it has been discussed in class. Questions are not taken from the text of the assigned book but are rather created from what we have discussed in class.

Cheating is not advisable. To reduce the incentives and temptations to cheat, the book is closed book, closed notes, no outside written or digital resources are allowed, no laptops, no cellphones, no personal digital assistants, no calculators, no clear water bottles and no hats are allowed during the exam period.

If you arrive to the exam period after the first person has turned in their exam, you will not be allowed to take the midterm exam and you will receive a zero for the exam.

Please consider this a representative list of the topics we have discussed and the questions to be representative of the average level of difficulty. There may be topics we discussed in class that are not included in this document, *caveat emptor*.

Topics included:

1. Introductory comments – definition of international trade, discussion about what trade theory is concerned and how it fits in the broader field of economics.
2. Microeconomics review – brief review of supply and demand, equilibrium concept, marginal benefit = marginal cost condition.
3. Ricardian Trade – distinction between absolute and comparative advantage, derivation of Ricardian trade model, measure of opportunity cost, how trade can make countries better off (consumption vs. production possibilities frontier), ranges of prices at which mutually beneficial trade might occur, determination of the pattern of trade.
4. Extensions to Ricardo – Factor endowment theory (Abundant factors stand to gain from trade), specific factors theory (specific factors stand to gain if they are specific to the exporting sector), factor-price equalization; inter vs. intra-industry trade; economies of scale (internal vs. external) as a reason for trade; overlapping demand models; product life-cycle models.
5. Trade Policy I – review of supply and demand, consumer and producer surplus, motivation for trade in a partial equilibrium framework (two countries, one good, small country assumption, common currency); comparison of autarky surplus to free-trade surplus; impact of a tariff on consumer surplus, producer surplus, government revenue; political economy of tariffs – who stands to gain, lose, and why restricted trade might prevail.

Review Questions for ECON3171 [Note: answers are not provided, nor will they be]

The table below shows the bushels of corn and the bottles of wine that Japan and Korea can produce per day of labor under four different hypothetical situations (Cases I – IV).

	Case I		Case II	
	Japan	Korea	Japan	Korea
Corn (bushels)	4	1	3	1
Wine (bottles)	1	2	4	2

1. Which country has an absolute advantage in producing corn in Case I?
2. Which country has an absolute advantage in producing wine in Case I?
3. Which country has an absolute advantage in producing wine in Case II?
4. Which country has a comparative advantage in producing wine in Case II?
5. What is the relative price of corn in Japan prior to trade in Case II?

The next set of questions is based upon the table below. The first two columns give the maximum daily amounts of steel and aluminum that France and Canada can produce when they completely specialize in one or other product. Production occurs under constant cost conditions. The last two columns give each country's consumption in autarky.

	Maximum steel production	Maximum aluminum production	Steel consumption in autarky	Aluminum consumption in autarky
Canada	500 tons	1500 tons	300 tons	600 tons
France	1200 tons	800 tons	600 tons	400 tons

6. What is the Canadian price of steel in autarky?
7. In which product does Canada have its comparative advantage?
8. If the international terms of trade settle at a level that is between autarkic prices in each country, then:
 - A. There is no basis for gainful trade for either country
 - B. Both countries gain from trade
 - C. Only one country gains from trade
 - D. One country gains and the other country loses from trade
9. The export of capital-intensive chemicals from US to China in exchange for imports of labor-intensive shoes is best explained as an illustration of:
 - A. Intra-industry trade.
 - B. Ricardian comparative advantage
 - C. The Heckscher-Ohlin Theorem or factor proportions theory.
 - D. Linder's theory of overlapping demands.

Use the table below to answer the next two questions.

US capital-labor ratios in selected industries

Industry	K/L (\$/worker)
Apparel and other textile products	\$8,274
Leather and leather products	\$12,466
Furniture	\$21,736
Lumber and wood products	\$39,134
Textile mill products	\$44,060
Electronic and electric equipment	\$54,582
Primary metal industries	\$123,594
Paper and allied products	\$171,730
Chemicals and allied products	\$192,593

10. Which industry is the most labor intensive?
 - A. Apparel
 - B. Lumber
 - C. Primary metal industries
 - D. Chemicals
11. Suppose that the US is labor abundant relative to Canada. Which of the following products is the US most likely to import from Canada?
 - A. Furniture
 - B. Textile mill products
 - C. Primary metal industries
 - D. Paper and allied products
12. Wages are generally _____?
 - A. Higher in labor abundant countries than in capital abundant countries.
 - B. Lower in labor abundant countries than in capital abundant countries.
 - C. The same in both labor abundant and capital abundant countries.
 - D. Have no relationship to labor abundance.

Use this information to answer the next four questions:

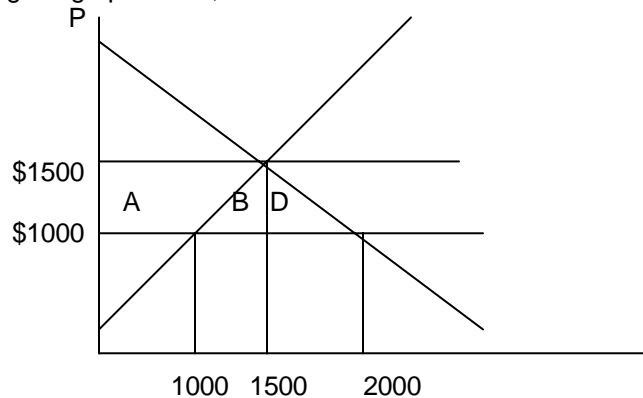
- France and Italy only trade with one another.
 - Each produces wine and bread.
 - The production of bread is relatively capital intensive and the production of wine is relatively labor intensive.
 - France is relatively abundant in capital and Italy is relatively abundant in labor.
13. Which statement below is correct?
 - A. Italy has a larger labor force than France.
 - B. France has a larger labor force than Italy.
 - C. The ratio of Italy's total capital stock to its labor force is smaller than the same ratio for France.
 - D. The ratio of the Italy's total capital stock to its labor force is larger than the same ratio for France.
 14. According to the Heckscher-Ohlin-Samuelson (HOS) factor proportions theory, what product will Italy export?
 - A. Bread
 - B. Wine
 - C. Both bread and wine
 - D. Neither bread nor wine
 15. According to the HOS factor proportions theory, free trade between Italy and France should cause:
 - A. A decrease in the French price of wine and a decrease in the Italian price of wine.
 - B. Increases in the price of wine in Italy and in France.

- C. An increase in the French price of wine and an increase in the Italian price of bread.
 - D. A decrease in the Italian price of bread and a decrease in the French price of wine.
16. According to the HOS factor proportions theory, free trade between France and Italy should result in:
- A. Increased wages in both countries.
 - B. Decreased wages in both countries.
 - C. Increased wages in France and increased returns to capital in Italy.
 - D. Increased returns to capital in France and increased wages in Italy.
17. Which of the following suggests that a nation will export the commodity in the production of which a great deal of its relatively abundant and cheap factor is used?
- A. The Linder theory
 - B. The product life cycle theory
 - C. The MacDougall theory
 - D. The Hecksher-Ohlin-Samuelson theory
18. According to Staffan Linder, trade between two countries tends to be *most* pronounced when the countries:
- A. Find their tastes and preferences to be quite harmonious
 - B. Experience economies of large-scale production over large output levels
 - C. Face dissimilar relative abundances of the factors of production
 - D. Find their per capita income levels to be approximately the same
19. A firm is said to enjoy economies of scale over the range of output for which average cost is:
- A. Increasing
 - B. Constant
 - C. Decreasing
 - D. None of the above
20. Which of the following suggests that by widening the market's size, international trade can permit larger production runs for manufacturers, which leads to increasing efficiency?
- A. Economies of scale
 - B. Diseconomies of scale
 - C. Comparative cost theory
 - D. Absolute cost theory
21. The theory of overlapping demands predicts that trade in manufactured goods is *unimportant* for countries with very different:
- A. Tastes and preferences
 - B. Expectations of future interest rate levels
 - C. Per-capita income levels
 - D. Labor productivities
22. The simultaneous import and export of computers by Germany is an example of:
- A. Intraindustry trade
 - B. Interindustry trade
 - C. Perfect competition
 - D. Imperfect competition
23. Which of the following should occur after labor emigrates from a labor abundant country to a capital abundant country?
- A. Wages should rise in the labor abundant country and fall in the capital abundant country.
 - B. Wages should rise in the capital abundant country and fall in the labor abundant country.
 - C. Returns to capital should rise in both countries.
 - D. Returns to capital should fall in both countries.

24. The difference between the price consumers are willing to pay and the price that they actually pay is known as:
- Price discrimination
 - Consumers surplus
 - Government surplus
 - Producers surplus
25. The US imposes a 32% tariff on imported cotton polyester blend knitted t-shirts. Which group below is likely to benefit the most from this tariff?
- Foreign t-shirt consumers
 - US t-shirt consumers
 - US t-shirt producers
 - Foreign t-shirt producers
 - All of the above.

The next three questions are based upon this information: Sweden is a small country that cannot influence the world price of laptop computers, which is \$1,000. Currently, it produces 1,000 computers and imports 1,000 computers. Now suppose that it imposes a tariff of \$500 on imported laptops. With the tariff, it produces 1500 computers and imports no computers.

26. Using the graph below, calculate the total consumer costs associated with the tariff.



- How many laptops does Sweden produce after it imposes the tariff?
- What is the dead-weight-loss of the tariff?
- What is the production inefficiency imposed by the tariff?
- What is the consumption inefficiency imposed by the tariff?

Use the table below, which gives the hypothetical supply and demand of television sets in Venezuela, to answer the next set of questions. Venezuela is a small country that is unable to affect world prices. The world price (free trade price) is \$200 per TV.

Price/TV set	Quantity Demanded	Quantity Supplied
\$100	2000	0
\$200	1600	400
\$300	1400	800
\$400	1200	1200
\$500	1000	1600
\$600	800	2000

- How many TV sets will Venezuela import if there are no trade barriers?
- How many TV sets will Venezuela TV producers supply if there are no trade barriers?
- Now suppose that Venezuela imposes a 100% tariff on imported TVs. How many TV sets will it now import?
- Who will benefit from Venezuela's 100% tariff on imported TVs?

35. A small country produces wheat and imports wheat. If it imposes a tariff on imported wheat, then:
- a. The price of imported wheat increases but the price of domestically produced wheat does not change.
 - b. The price of imported wheat does not change but the price of domestically produced wheat increases.
 - c. The prices of imported wheat and domestically produced wheat both decrease.
 - d. The prices of imported wheat and domestically produced wheat both increase.
36. A tariff on imported T-shirts cause a redistribution of income from:
- a. The government to T-shirt producers and T-shirt consumers.
 - b. T-shirt consumers and the government to T-shirt producers.
 - c. T-shirt producers and T-shirt consumers to the government.
 - d. T-shirt consumers to T-shirt producers and the government.
37. The activity of US textile producers seeking higher tariffs is known as:
- a. Multilateral trade negotiations.
 - b. Bi-lateral trade negotiations.
 - c. Rent seeking activity.
 - d. Broad focus tariff policy activity.
38. The deadweight loss of a tariff:
- a. Is a social loss since it promotes inefficient production
 - b. Is a social loss since it reduces the revenue for the government
 - c. Is not a social loss because society as a whole doesn't pay for the loss
 - d. Is not a social loss since only business firms suffer revenue losses
39. A decrease in the import tariff will result in a(n):
- a. Increase in imports but a decrease in domestic production
 - b. Decrease in imports but an increase in domestic production
 - c. Increase in price but a decrease in quantity purchased
 - d. Decrease in price and a decrease in quantity purchased