Exam 2 _ Study Guide
ECON 4190: International Economics & Globalization

The second exam includes 26 True/False and multiple-choice questions where 2 or 3 of these are from in-class presentations (each worth 1.5 points for a total of %39 of the grade). There are also 4 explanatory questions for which you need to show graphing and calculations (%61 of the grade). You will have 80 minutes time limit to answer all the questions. ***Don't forget to bring a calculator.***

Chapters 6 to 10 and 14 are included in the exam. Study the book, PPT slides, your notes, online homeworks, and group assignments, as well as the sample questions included in this study guide. Make sure to study all the material and understand the concepts.

Sample Questions

1. Assume a firm has monopoly both at Home and in Foreign.

   a. Home's demand curve for the product is P = \$100 - 0.5Q (Q is measured in millions of goods), while Foreign's demand is P* = \$50 - 0.1Q*. Assume the marginal cost at home is a constant MC = \$10, but there is a \$4 shipping cost to Foreign so MC* = \$14. Solve for the profit-maximizing prices P and P*, as well as the profit-maximizing quantities Q and Q*. If you don't know calculus, just remember that marginal revenue is twice as steep as demand.
   b. Assume the firm's fixed cost is a total of \$4000 (millions) and solve for total profit from Home and Foreign sales.

2. Consider a small country with a domestic oil monopoly and rising marginal costs.

   a. Assuming demand is linear, show the monopoly's demand, marginal cost, and marginal revenue curves. Show how the monopoly's profit-maximizing price and quantity (Pm, Qm) compare to those under perfect competition (Pc, Qc).
   b. On a new diagram, suppose that the country can now import oil at a world price below Pc. Show its imports. Relative to the monopoly equilibrium, how would free trade affect consumer and producer surplus in the oil market?

3. Suppose that Home's domestic market for shoes is perfectly competitive. Demand and supply are linear, so every time price changes by $1, quantity-demanded changes by 30 million and quantity-supplied changes by 20 million. At the current free-trade price of $60, Home produces 500 million pairs per year, and imports 3 billion pairs.

a. Find the supply and demand equations and solve for Home's equilibrium price and quantity.
b. Solve P when S=0 and when D=0 in order to find the vertical intercepts, and draw the supply and demand diagram. Solve for both consumer surplus and producer surplus at the equilibrium price and quantity.
c. Now consider the free-trade price of $60 and solve for consumer surplus and producer surplus. Do you see a decrease or increase in each of them?

Assume that Home is a very small part of the world shoe market, and Home's government imposed a $10 tariff on imported shoes.

d. Solve for the new domestic P, quantity-supplied, quantity-demanded, and quantity of shoes imported.
e. Solve for welfare effects of the tariff comparing to the free trade situation by showing the changes in Home's consumer surplus, producer surplus, and the government revenue on a graph. What is the total change in Home's welfare?

Assume in the above case that Home is instead a large part of the world's shoe market, and suppose that Home now imposes a $15 tariff, which makes the domestic price rise by $10 but decreases the world price by $5.

f. Calculate the changes in Home's total welfare from this tariff comparing to the free trade situation.

4. Assume that the euro interest rate is constant at 5 percent, and that the expected exchange rate is 1.05 dollars per one euro. Find the expected dollar return on euro deposits for the following cases.

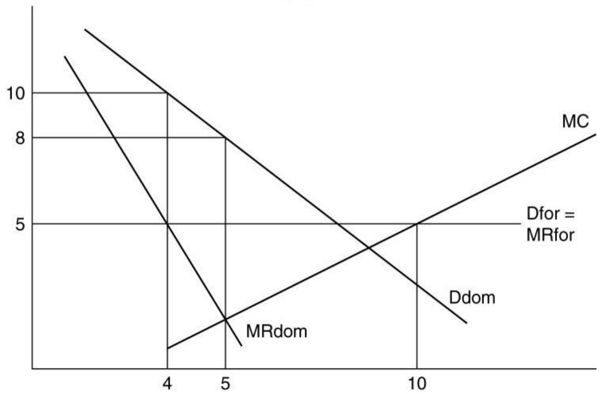
Case	Today's Dollar/Euro Exchange Rate	Interest Rate on Euro Deposits	Expected Dollar Depreciation Rate Against Euro (1.05 – E)/E	Expected Dollar Return on Euro Deposits Re + (1.05 – E)/E
1	1.07			
2	1.06			
3	1.05			
4	1.04			
5	1.03			
6	1.02			
7	1.01			
8	1			
9	0.99			
10	0.98			

Multiple-Choice Sample Questions

1) Tastes of individuals are represented by
A) isovalue lines.
B) production possibility frontiers.
C) production functions.
D) indifference curves.
E) the terms of trade.

2) An import tariff will cause the relative demand for ________ to ________ and the relative supply for ________ to ________.
A) exports; decrease; exports; increase
B) imports; increase; imports; decrease
C) exports; increase; exports; decrease
D) imports; decrease; imports; increase
E) exports; increase; imports; decrease

3) Refer to the figure below. Assume that the domestic monopolist can export as much as it likes of its steel at the world competitive price. How much steel will the monopolist sell, and at what price?



A) It would sell 10 million tons at $10/ton.
B) It would sell 10 million tons at $5/ton.
C) It would sell 5 million tons at $10/ton.
D) It would sell 5 million tons at $8/ton.
E) It would sell 4 million tons at $10/ton.

4) When there are external economies of scale, an increase in the size of the market will
A) not affect the number of firms, but will 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) increase the number of firms and lower the price per unit.

5) If some industries exhibit internal increasing returns to scale in each country, we should not expect to see
A) intra-industry trade between countries.
B) high levels of specialization in both countries.
C) inter-industry trade between countries.
D) perfect competition in these industries.
E) increased productivity in both countries.

6) The long-run market supply curve in the presence of internal economies of scale is ________, and in the presence of external economies of scale, it is ________.
A) horizontal; upward sloping
B) downward sloping; downward sloping
C) upward sloping; downward sloping
D) upward sloping; horizontal
E) downward sloping; horizontal

7) In the presence of external economies of scale, trade
A) will unambiguously improve welfare in both countries.
B) will unambiguously worsen welfare in the exporting country and improve welfare in the importing country.
C) may or may not improve welfare in both countries.
D) will unambiguously improve welfare in the exporting country and worsen welfare in the importing country.
E) will unambiguously worsen welfare in both countries.

8) If a firm increases its output in the ________ and unit costs ________, then the firm is experiencing ________ of scale.
A) short run; decrease; economies
B) long run; increase; diseconomies
C) short run; decrease; diseconomies
D) long run; increase; economies
E) long run; decrease; diseconomies

9) A product is produced in a monopolistically competitive industry with scale economies. If this industry exists in two countries, and these two countries engage in trade with each other, then we would expect
A) the country with a relative abundance of the factor of production in which production of the product is intensive will export this product.
B) the countries will trade only with other nations they are not in competition with.
C) the country in which the price of the product is lower will export the product.
D) neither country will export this product since there is no comparative advantage.
E) each country will export different varieties of the product to the other.

10) If a firm that uses a production process that yields economies of scale charges a price less than ________, then profit will be ________.
A) marginal cost; positive
B) average cost; negative
C) marginal revenue; positive
D) marginal cost; maximized
E) marginal revenue; maximized

11) An imperfectly competitive firm has the following demand curve: $Q = 100 - 2P$. What is marginal revenue equal to when $P = 30$?
A) 70
B) 40
C) 10
D) 30
E) 40

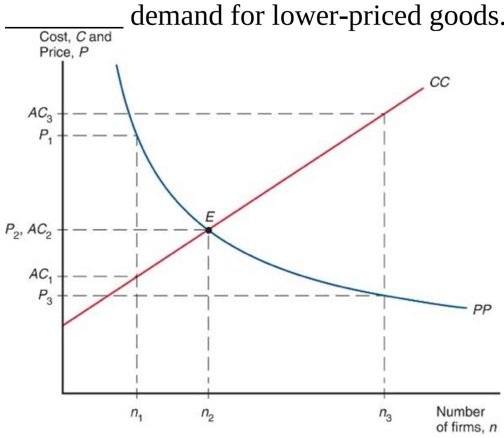
12) An imperfectly competitive firm has the following total cost curve: C = 100 + 4Q. What are the marginal cost and average cost respectively when Q = 10?
A) 14 & 140
B) 4 & 140
C) 4 & 14
D) 100 & 140
E) 100 & 14

13) The simultaneous export and import of widgets by the United States is an example of
A) inter-industry trade.
B) imperfect competition.
C) the effect of a monopoly on international trade.
D) intra-industry trade.
E) increasing returns to scale.

14) Complaints are often made to the International Trade Commission concerning foreign "dumping" practices. These complaints typically claim that
A) foreign companies are charging prices that are lower than prices they charge countries other than the U.S.
B) foreign companies are charging exorbitant prices that are higher than the true value of the products.
C) U.S. consumers cannot differentiate between the foreign and domestic goods.
D) U.S. firms are harmed by the unfair pricing of foreign exporters.
E) U.S. consumers are harmed by the lack of quality control or health concerns in foreign

15) In the model of monopolistic competition, trade costs between countries cause
A) marginal costs of exported goods to exceed the marginal costs of goods sold domestically.
B) all firms that can earn a profit on domestic sales to export their goods at higher prices.
C) countries to negotiate the elimination of trade costs by mutual subsidization of trade.
D) marginal costs of goods sold domestically to exceed the marginal costs of exported goods.
E) all firms that can earn a profit on domestic sales to export their goods at lower prices.

16) Refer to the figure below. In the model of monopolistic competition, an increase in industry size will cause the *CC* curve to become ________, which will ________ demand for higher-priced goods and ________ demand for lower-priced goods.



A) steeper; reduce; increase
B) steeper; increase; reduce
C) horizontal; reduce; reduce
D) flatter; increase; reduce
E) flatter; reduce; increase

17) A tax of 20 cents per unit of imported garlic is an example of a(n)
A) specific tariff.
B) *ad valorem* tariff.
C) nominal tariff.
D) effective protection tariff.
E) a disadvantageous tariff.

18) The most vocal political pressure for tariffs is generally made by
A) consumers lobbying for export tariffs.
B) consumers lobbying for import tariffs.
C) consumers lobbying for lower import tariffs.
D) producers lobbying for export tariffs.
E) producers lobbying for import tariffs.

19) The main redistribution effect of a tariff is the transfer of income from
A) domestic producers to domestic buyers.
B) domestic buyers to domestic producers.
C) domestic producers to domestic government.
D) domestic government to domestic consumers.
E) foreign producers to domestic consumers.

20) Should the home country be "large" relative to its trade partners, its imposition of a tariff on imports would lead to an increase in domestic welfare if the terms of the trade rectangle exceed the sum of the
A) revenue effect plus redistribution effect.
B) protective effect plus revenue effect.
C) consumption effect plus redistribution effect.
D) production distortion effect plus consumption distortion effect.
E) terms of trade gain.

21) If the goods' money prices do NOT change, a depreciation of the dollar against the pound
A) makes British sweaters cheaper in terms of American jeans.
B) makes British sweaters more expensive in terms of American jeans.
C) makes American jeans more expensive in terms of British sweaters.
D) doesn't change the relative price of sweaters and jeans.
E) makes British jeans more expensive in Britain.

22) Which one of the following statements is the MOST accurate?
A) Spot exchange rates are always higher than forward exchange rates.
B) Spot exchange rates are always lower than forward exchange rates.
C) Spot exchange rates and forward exchange rates are always equal.
D) Spot exchange rates and forward exchange rates are equal when the value date and the date of the spot transaction are the same.
E) Spot exchange rates and forward exchange rates never move closely together.

23) A foreign exchange swap
A) is a spot sale of a currency.
B) is a forward repurchase of the currency.
C) is a spot sale of a currency combined with a forward repurchase of the currency.
D) is a spot sale of a currency combined with a forward sale of the currency.
E) make up a negligible proportion of all foreign exchange trading.

24) If the dollar interest rate is 10 percent, the euro interest rate is 12 percent, then
A) an investor should invest only in dollars if the expected dollar appreciation against the euro is 4 percent.
B) an investor should invest only in euros. An investor should invest only in dollars if the expected dollar appreciation against the euro is 4 percent.
C) an investor should be indifferent between dollars and euros. An investor should invest only in dollars if the expected dollar appreciation against the euro is 4 percent.
D) an investor should invest only in dollars.
E) an investor should invest only in euros.

25) The dollar rate of return on euro deposits is
A) approximately the euro interest rate plus the rate of depreciation of the dollar against the euro.
B) approximately the euro interest rate minus the rate of depreciation of the dollar against the euro.
C) the euro interest rate minus the rate of inflation against the euro.
D) the rate of appreciation of the dollar against the euro.
E) the euro interest rate plus the rate of inflation against the euro.

Answer Key

1) D
2) D
3) B
4) E
5) D
6) B
7) C
8) B
9) E
10) B
11) C
12) C
13) D
14) D
15) A
16) E
17) A
18) E
19) B
20) D
21) B
22) D
23) C
24) A
25) A