FOREIGN DIRECT INVESTMENT

1. That BMW produces its compact sports utility vehicles in the United States to be close to its largest consumer base and thus reduce trade costs is an example of:
   a) horizontal FDI
   b) vertical FDI
   c) diagonal FDI
   d) circular FDI
   e) export platform FDI

2. That Volkswagen produces its engines in Germany but many of its passenger cars in the United States is an example of:
   a) horizontal FDI
   b) vertical FDI
   c) diagonal FDI
   d) circular FDI
   e) export platform FDI

3. For 2014, while developed countries and economies in transition saw a _________, inflows to developing economies __________.
   a) significant increase, saw a slight decrease
   b) slight decrease, saw a slight increase
   c) significant decrease, remained at historically high levels
   d) significant decrease, saw a significant increase
   e) none of the above

4. For 2014, the United States was no longer the country receiving the largest amount of inward FDI. That honor went to
   a) Canada
   b) China
   c) Singapore
   d) United Kingdom
   e) none of the above
5-12 France has imposed import quotas limiting American films to 40% of television screenings and 60% in theaters. Ignore the issue of cultural identity in answering the following questions.

5. The import quota causes consumer surplus in France to
   a) rise due to the French price of films rising
   b) rise due to the French price of films falling
   c) remains the same
   d) fall due to the French price of films rising
   e) fall due to the French price of films falling

6. The import quota causes producer surplus in France to
   a) rise due to the French price of films rising
   b) rise due to the French price of films falling
   c) remains the same
   d) fall due to the French price of films rising
   e) fall due to the French price of films falling

7. The import quota on American films creates a ____________ in France due to too many French films being made.
   a) second best equilibrium
   b) consumption distortion
   c) production distortion
   d) terms of trade gain
   e) none of the above

8. The import quota on American films creates a ____________ in France due to too few films being consumed.
   a) second best equilibrium
   b) consumption distortion
   c) production distortion
   d) terms of trade gain
   e) none of the above
9-12 Suppose Italy removes an export subsidy on pasta. Italy is large enough for its policies to affect the world price for pasta.

9. Italy removing its export subsidy causes the quantity demanded of pasta and consumer surplus in Italy to
   a) rise due to the Italian price of pasta rising
   b) rise due to the Italian price of pasta falling
   c) remains the same
   d) fall due to the Italian price of pasta rising
   e) fall due to the Italian price of pasta falling

10. Italy removing its export subsidy causes the quantity supplied of pasta and producer surplus in Italy to
    a) rise due to the Italian price of pasta rising
    b) rise due to the Italian price of pasta falling
    c) remains the same
    d) fall due to the Italian price of pasta rising
    e) fall due to the Italian price of pasta falling

11. Italy removing its export subsidy causes the quantity demanded of pasta and consumer surplus in the ROW to
    a) rise due to the ROW price of pasta rising
    b) rise due to the ROW price of pasta falling
    c) remains the same
    d) fall due to the ROW price of pasta rising
    e) fall due to the ROW price of pasta falling

12. Italy removing its export subsidy causes the quantity supplied of pasta and producer surplus in the ROW to
    a) rise due to the ROW price of pasta rising
    b) rise due to the ROW price of pasta falling
    c) remains the same
    d) fall due to the ROW price of pasta rising
    e) fall due to the ROW price of pasta falling
POLITICAL ECONOMY OF TRADE POLICY

13. If a domestic market, such as the labor market, fails to function properly, deviating from free trade
   a) is always a good idea
   b) can sometimes help correct the existing distortion if a more targeted policy is not feasible
   c) should be used in addition to more targeted policies as manipulating two different policies ensures a better outcome
   d) is never a good idea as free trade is ALWAYS best
   e) none of the above

14. Although a country could improve their terms of trade (buy imports cheaper) by adopting an import tariff, the country would
   a) run the risk of provoking retaliation by trading partners
   b) likely not generate much of a terms of trade improvement unless they are a large country
   c) generate efficiency losses through consumption and production distortions due to the price rising
   d) expose their government to protectionist pressure from industry lobbies even when the policy does not improve national welfare
   e) all of the above

15. As a percentage of GDP, who stands to gain the most from a move to free trade?
   a) United States
   b) European Union
   c) Japan
   d) developing countries
   e) world as a whole

16. Free trade areas and customs unions could be harmful due to trade diversion, the replacement of low cost imports from _________ with higher cost goods from _________.
   a) outside the zone; member countries
   b) member countries; outside the zone
   c) member countries; domestic production
   d) outside the zone; domestic production
   e) none of the above
TRADE POLICY PROBLEMS

In the United States (US), inverse demand is $P = 20 - 2Q_D$, while inverse supply is $P = 4 + 2Q_S$. In the rest of the world (ROW), inverse demand is $P^* = 16 - 2Q_D^*$, while inverse supply is $P^* = 2 + 2Q_S^*$.

17. The US autarky price is $P^a =$
   a) 12
   b) 11
   c) 10
   d) 9
   e) none of the above

18. US quantity demanded is $Q_D =$
   a) $-10 - \frac{1}{2} P$
   b) $-10 + \frac{1}{2} P$
   c) $10 + \frac{1}{2} P$
   d) $10 - \frac{1}{2} P$
   e) none of the above

19. US quantity supplied is $Q_S =$
   a) $-2 - \frac{1}{2} P$
   b) $-2 + \frac{1}{2} P$
   c) $2 + \frac{1}{2} P$
   d) $2 - \frac{1}{2} P$
   e) none of the above

20. US import demand is $M =$
   a) $-12 - P$
   b) $-12 + P$
   c) $8 + P$
   d) $8 - P$
   e) none of the above

21. US import demand has price intercept ____ and slope ____.
   a) 12, -1
   b) 12, 1
   c) -8, 1
   d) -8, -1
   e) none of the above
22. The ROW autarky price is $P^* =$
   a) 12
   b) 11
   c) 10
   d) 9
   e) none of the above

23. ROW quantity demanded is $Q_D^* =$
   a) $8 + (\frac{1}{2}) P^*$
   b) $9 - (\frac{1}{2}) P^*$
   c) $-8 + (\frac{1}{2}) P^*$
   d) $-8 - (\frac{1}{2}) P^*$
   e) none of the above

24. ROW quantity supplied is $Q_S^* =$
   a) $1 - (\frac{1}{2}) P^*$
   b) $-1 + (\frac{1}{2}) P^*$
   c) $1 + (\frac{1}{2}) P^*$
   d) $-1 - (\frac{1}{2}) P^*$
   e) none of the above

25. ROW export supply is $X^* =$
   a) $9 - P^*$
   b) $-9 + P^*$
   c) $7 + P^*$
   d) $-7 - P^*$
   e) none of the above

26. ROW export supply has price intercept ___ and slope ____.
   a) 9, -1
   b) 9, 1
   c) -7, -1
   d) -7, 1
   e) none of the above
27. The free trade price is $P = \)
   a) 12
   b) 11
   c) 10
   d) 9
   e) none of the above

28. US imports under free trade are $M = \)
   a) 5/2=2.5
   b) 2
   c) 3/2=1.5
   d) 1
   e) none of the above

29. US quantity demanded under free trade is $D = \)
   a) 19/4=4.75
   b) 9/2=4.5
   c) 7/2=3.5
   d) 13/4=3.25
   e) none of the above

30. US quantity supplied under free trade is $S = \)
   a) 19/4=4.75
   b) 9/2=4.5
   c) 7/2=3.5
   d) 13/4=3.25
   e) none of the above

31. The US tariff-ridden import demand for a specific tariff $t = 1$ is $M_T = \)
   a) 11 - P*
   b) -11 + P*
   c) -11 - P*
   d) 11 + P*
   e) none of the above
32. It has price intercept ___ and slope ____.
   a) 11, -1
   b) 12, 1
   c) -12, -1
   d) -13, 1
   e) none of the above

33. The ROW price with the tariff is
   a) 12
   b) 11
   c) 10
   d) 9
   e) none of the above

34. The US price with the tariff is
   a) 12
   b) 11
   c) 10
   d) 9
   e) none of the above

35. US imports with the tariff are
   a) 5/2=2.5
   b) 2
   c) 3/2=1.5
   d) 1
   e) none of the above

36. US quantity demanded with the tariff is $D_2 =$
   a) 19/4=4.75
   b) 9/2=4.5
   c) 7/2=3.5
   d) 13/4=3.25
   e) none of the above
37. US quantity supplied with the tariff is $S_2 =$
   a) $19/4 = 4.75$
   b) $9/2 = 4.5$
   c) $7/2 = 3.5$
   d) $13/4 = 3.25$
   e) none of the above

38. How large of a tariff would the United States need to impose to prohibit all imports?
   a) 4
   b) 3
   c) 2
   d) 1
   e) none of the above

39. The change in US consumer surplus due to the tariff is
   a) $-37/16 = -2.3125$
   b) $-27/16 = -1.6875$
   c) $27/16 = 1.6875$
   d) $37/16 = 2.3125$
   e) none of the above

40. The change in US producer surplus due to the tariff is
   a) $-37/16 = -2.3125$
   b) $-27/16 = -1.6875$
   c) $27/16 = 1.6875$
   d) $37/16 = 2.3125$
   e) none of the above

41. The government revenue collected in the United States due to the tariff is
   a) $5/2 = 2.5$
   b) 2
   c) $3/2 = 1.5$
   d) 1
   e) none of the above
42. The US consumption distortion created by the tariff is
   a) 1/2
   b) 1/4
   c) 1/8
   d) 1/16
   e) none of the above

43. The US production distortion created by the tariff is
   a) 1/2
   b) 1/4
   c) 1/8
   d) 1/16
   e) none of the above

44. The US efficiency loss is
   a) 1/2
   b) 1/4
   c) 1/8
   d) 1/16
   e) none of the above

45. The US efficiency loss occurs because the United States produces
   ____ and consumes _____ due to the tariff.
   a) too much, too much
   b) too much, too little
   c) too little, too much
   d) too little, too little
   e) none of the above

46. The US terms of trade gain is
   a) 1/2
   b) 1/4
   c) 1/8
   d) 1/16
   e) none of the above
47. The US terms of trade gain occurs because the United States ____ due to the tariff.
   a) buys imports cheaper
   b) buys more imports
   c) buys fewer imports
   d) has no effect on the ROW price
   e) none of the above

48. The change in welfare in the United States due to the tariff is
   a) 1/2
   b) 3/8
   c) 1/4
   d) -1/4
   e) none of the above

49. Compared to free trade, is the United States better or worse off with this tariff?
   a) better with this tariff
   b) worse with this tariff
   c) the same with this tariff as with free trade
   d) none of the above
   e) cannot tell from the information provided

50. Why? Because the ________ outweighs the ______ for a large country (able to affect world prices) adopting a small tariff starting from free trade.
   a) terms of trade gain, efficiency loss
   b) efficiency loss, terms of trade gain
   c) production distortion, consumption distortion
   d) consumption distortion, production distortion
   e) none of the above
1a That BMW produces its compact sports utility vehicles in the United States to be close to its largest consumer base and thus reduce trade costs is an example of horizontal FDI.

2b That Volkswagen produces its engines in Germany but many of its passenger cars in the United States is an example of vertical FDI.

3c For 2014, while developed countries and economies in transition saw a significant decrease, inflows to developing economies remained at historically high levels.

4b For 2014, the United States was no longer the country receiving the largest amount of inward FDI. That honor went to China.

5d The import quota causes consumer surplus in France to fall due to the French price of films rising.

6a The import quota causes producer surplus in France to rise due to the French price of films rising.

7c The import quota on American films creates a production distortion in France due to too many French films being made.

8b The import quota on American films creates a consumption distortion in France due to too few films being consumed.

9b Italy removing its export subsidy causes the quantity demanded of pasta and consumer surplus in Italy to rise due to the Italian price of pasta falling.

10e Italy removing its export subsidy causes the quantity supplied of pasta and producer surplus in Italy to fall due to the Italian price of pasta falling.

11d Italy removing its export subsidy causes the quantity demanded of pasta and consumer surplus in the ROW to fall due to the ROW price of pasta rising.

12a Italy removing its export subsidy causes the quantity supplied of pasta and producer surplus in the ROW to rise due to the ROW price of pasta rising.
13b If a domestic market, such as the labor market, fails to function properly, deviating from free trade can sometimes help correct the existing distortion if a more targeted policy is not feasible.

14e Although a country could improve their terms of trade (buy imports cheaper) by adopting an import tariff, the country would run the risk of provoking retaliation by trading partners, likely not generate much of a terms of trade improvement unless they are a large country, generate efficiency losses through consumption and production distortions due to the price rising, and expose their government to protectionist pressure from industry lobbies even when the policy does not improve national welfare (all of the above).

15d As a percentage of GDP, developing countries stand to gain the most from a move to free trade.

16a Free trade areas and customs unions could be harmful due to trade diversion, the replacement of low cost imports from outside the zone with higher cost goods from member countries.

17a The US autarky price is $P^A = 12$
18d US quantity demanded is $Q_D = 10 - (\frac{1}{2}) P$
19b US quantity supplied is $Q_S = -2 + (\frac{1}{2}) P$
20e US import demand is $M = 12 - P$ (none of the above)
21a US import demand has price intercept 12 and slope -1.

22d The ROW autarky price is $P^A^* = 9$
23e ROW quantity demanded is $Q_D^* = 8 - (\frac{1}{2}) P^*$ (none of the above)
24b ROW quantity supplied is $Q_S^* = -1 + (\frac{1}{2}) P^*$
25b ROW export supply is $X^* = -9 + P^*$
26b ROW export supply has price intercept 9 and slope 1.

27e The free trade price is $P = 21/2 = 10.5$ (none of the above)
28c US imports under free trade are $M = 3/2 = 1.5$
29a US quantity demanded under free trade is $D^f = 19/4 = 4.75$
30d US quantity supplied under free trade is $S^f = 13/4 = 3.25$

31a The US tariff-ridden import demand for a specific tariff $t = 1$ is $M_T = 11 - P^*$
32a It has price intercept 11 and slope -1.
33c The ROW price with the tariff is 10
34b The US price with the tariff is 11
35d US imports with the tariff are $M_T = 1$
36b US quantity demanded with the tariff is \( D_2 = \frac{9}{2} = 4.5 \)
37c US quantity supplied with the tariff is \( S_2 = \frac{7}{2} = 3.5 \)
38b How large of a tariff would the United States need to impose to prohibit all imports? 3

39a The change in US consumer surplus due to the tariff is \( \Delta CS = -\frac{37}{16} = -2.3125 \)
40c The change in US producer surplus due to the tariff is \( \Delta PS = \frac{27}{16} = 1.6875 \)
41d The government revenue collected in the United States due to the tariff is 1

42d The US consumption distortion created by the tariff is \( \frac{1}{16} \)
43d The US production distortion created by the tariff is \( \frac{1}{16} \)
44c The US efficiency loss is \( \frac{1}{8} \)
45b The US efficiency loss occurs because the United States produces too much and consumes too little due to the tariff.
46a The US terms of trade gain is \( \frac{1}{2} \)
47a The US terms of trade gain occurs because the United States buys imports cheaper due to the tariff.

48b The change in welfare in the United States due to the tariff is \( \frac{3}{8} \)
49a Compared to free trade, is the United States better or worse off with this tariff? better with this tariff
50a Why? Because the terms of trade gain outweighs the efficiency loss for a large country (able to affect world prices) adopting a small tariff starting from free trade.