

ECON3315: INTERNATIONAL ECONOMIC ISSUES – Fall 2017

ASSIGNMENT 1 (Set and available Tuesday Oct 17th. DUE Tuesday October 31st in class)

1. Home has 1200 units of labor available. It can produce 2 goods, wine and cheese. The unit labor requirement in wine production is 6, while in cheese production it is 3.
 - a. Graph Home's PPF
 - b. What is the opportunity cost of wine in terms of cheese?
 - c. In autarky, what would the price of wine in terms of cheese be? Why?

2. Home is as described in Q1. Foreign, with a labor force of 800 has unit labor requirement in wine production of 4, while in cheese production it is 1.
 - a. Graph Foreign's PPF.
 - b. What is the opportunity cost of wine in terms of cheese for foreign?

3. Home and Foreign are as in Q1 and Q2. Assume that they now trade.
 - a. What will be the range of prices for trading wine and cheese between Home and Foreign?
 - b. Suppose both H and F decide to trade and fix prices at 3 units of cheese per unit of wine. Assuming both countries specialize, which country will produce which product and how much will they produce?
 - c. What are the gains from trade here? Assume that initially in autarky both countries were consuming half way down their PPCs.

4. "The world's poorest countries cannot find anything to export. There is no resource that is abundant – certainly not capital nor land, and in small poor nations not even labor is abundant." Discuss in the context of the Heckscher-Ohlin model.

5. Suppose two countries, Alphaland and Betaland have the following endowments of factors of production: Alphaland has 1200 labor and 300 machines and Betaland has 800 labor and 400 machines. Suppose there are two goods in the world, food and cellphones, where food production is labor intensive and cellphone production is capital intensive. Which country should produce which product and why?

6. It is often argued that the existence of increasing returns is a source of conflict between countries, since each country is better off, if it can increase its production in those industries characterized by economies of scale. Evaluate this view in terms of the Krugman/monopolistic competition model.

7. Who are in the winners and who are the losers in:
 - a. The Ricardian model?;
 - b. The Heckscher Ohlin model?; and
 - c. The Krugman model?

8. What is the difference between a free trade area and a customs union? What are the advantages and disadvantages of each?

9. Explain the difference between multilateral trade liberalization and bilateral or regional trade liberalization. How do these two types of trade liberalization coexist, and why has one of these types of trade liberalization been more prevalent in recent years?

10. What do you see as the advantages and disadvantages of the WTO?

11. What is the difference between a Free Trade Area (FTA) and a customs union (CU)? Why do you think the trade relations of specific countries that decide to join a preferential trade agreement (PTA, such as a FTA or CU) will help determine the preferences of the countries involved?

12. In the context of a PTA, explain the difference between trade creation and trade diversion and why this is important in terms of determining the welfare effects of a PTA.

Patrick Crowley, October 2017.