

FIRST IN-CLASS TEST

*Respond to all the questions below, writing **legibly** on these pages. The points noted by each question total 59. Since the test is worth 18 points towards the quarter's total of 100, I'll multiply your raw score by 0.305. Watch your spelling¹; I'll deduct 0.1 raw point for each incidence of each spelling error about which I've warned you. You have 110 minutes.*

A. SHORT ANSWER [20 points]

1. List the three countries that are the largest producers of agricultural products.
2. List the three countries that are the largest producers of manufactured goods.
3. List the three countries that are the largest producers of services.

Questions 4-6 refer to Table 1 on the next page.

4. Which row provides the broadest measure of the US "trade balance" in Table 1?
5. Rows (1) + (18) + (35) = - [(39) + (40) + (55) + (70) + (71)]. What principle does this illustrate?
6. In which detailed row would you enter each of the following transactions, and would the transaction be a negative or positive number? It is possible that the transaction would not register in a table of US international transactions.
 - a) A Mexican worker in the US sends \$1000 to his family in Mexico.
 - b) An American business woman flies to Taiwan on Singapore Airlines.
 - c) AT&T (US) pays a monthly fee to the Indian call-center company that handles its customer-service calls.
 - d) Bank of America establishes a new subsidiary in Brazil.
 - e) Boeing buys Global Aeronautica's 50% stake in the fuselage assembly plant in North Charleston, SC. Global Aeronautica is owned by an Italian company.

¹ Especially homophones (its/it's; there/they're/their), plurals, and possessives (countries/country's/countries').

- f) Boeing sells 50 planes to Japan Airlines.
- g) Ford of Mexico sells 50,000 automobile seats to a Ford assembly plant in Michigan.
- h) Ford (US) sells the Jaguar automobile line (Jaguar is headquartered in and has its manufacturing in the UK) to Tata, an Indian conglomerate.
- i) Microsoft Corp. (US) receives its dividend from its subsidiary in France.
- j) The Chinese government buys \$50M of US Treasury bonds.
- k) The US government forgives a \$20M loan to the Yemeni government.
- l) The US-based Fulbright organization pays the tuition for a US student at a Korean university.
- m) Wal-Mart (US) purchases 20,000 bicycles from a Mexican supplier.
- n) You buy a Chinese-made shirt from the Gap.
- o) You stay in a hotel in Vancouver BC.

TABLE 1

U.S. INTERNATIONAL TRANSACTIONS, 2009		
(all figures in millions of current U.S. dollars)		
<i>Source: Bureau of Economic Analysis, International Accounts Data, Balance of Payments Tables; http://www.bea.gov/international/bp_web/</i>		
1	Exports of goods, services, income	2,159,000
3	Goods	1,068,499
4	Services (travel, royalties, private services)	502,298
12	Income receipts (on U.S. assets abroad)	588,203
18	Imports of goods, services, income	-2,412,489
20	Goods	-1,575,443
21	Services (travel, transportation, royalties, private services, defense exp. abroad)	-370,262
29	Income payments (on foreign assets in U.S.)	-466,783
35	Unilateral transfers, net	-124,943
39	Capital account transactions, net	-140
40	U.S. assets abroad, net change	-140,465
51	US FDI abroad, net change	-268,680
55	Foreign assets in U.S., net change	305,736
64	FDI into the US, net change	134,707
70	Financial derivatives, net	50,804
71	Statistical discrepancy	162,497
	<i>Memoranda</i>	
72	Balance on goods = (3) + (20)	-506,944
73	Balance on services = (4) + (21)	132,036
74	Balance on goods and services = (71) + (72)	-374,908
77	Balance on current account = (1) + (18) + (35) = - [(39) + (40) + (55) + (70) + (71)]	-378,432

ESSAYS [39 points] *Please write in fairly large print, and use multiple paragraphs.*

1. [15 points] Why is the neoclassical theory of international trade a "deductive" theory? Why is it a "normative" theory? What basic question does it try to answer? How does it answer its basic question? (In your explanation, please use and define "opportunity costs," "comparative advantage," "factor proportions," and "gains from trade.") What are three of the key assumptions of this approach? What trade policy is implied by the theory? Explain how two of the key assumptions may sometimes not be met by reality. What policy implications can you derive from the discrepancy between each of those assumptions and reality?

2. [4 points] Describe two key ways in which "new trade theory" modifies the basic neoclassical model. What policies are implied by this modification of neoclassical trade theory?

3. [4 points] Explain one of the generalizations about world trade that we developed inductively. How can our deductively developed theory of trade explain that generalization?

4. [3 points] Interpret each of the three ratios on the right side of this formula:

$$G_1 = (A_1/B_2)(C_2/C_1) - a_1/b_1 ,$$

where

G_1 is the gain that Country 1 sees from exporting a unit of a

A & B are prices for those two products,

1 & 2 are countries,

C is a unit of currency (for Country 1 and Country 2), and

a & b are production costs of those two products.

5. [4 points] From the formula above, what are three ways for Country 1 to increase its gains from trade with Country 2? Which one of those ways does not reduce Country 2's gains from trade with Country 1?

6. [9 points] Describe three major factors that influence changes in the value of a country's currency relative to the currencies of its major trading partners. How does each influence operate (in other words, why does it usually affect exchange rates, and in what direction is the influence)?