Econ 188 – Exam 1 **NAME:_____**
Spring 2014 **ID:_____**
Professor Spearot

I have neither given nor received unauthorized aid on this examination, nor have I concealed any similar misconduct by others.

*Signature*_____

Part 1 (2 points each – circle one unless otherwise noted)

1. An iceberg trade cost is ____
    a. assessed per-unit
    b. assessed as a percentage of production value
    c. a fixed cost
    d. None of the above
2. Exported value from the US _____
    a. is concentrated in relatively few firms
    b. currently exceeds imported value
    c. 'a' and 'b'
    d. neither 'a' or 'b'
3. Most exporters in the US _____
    a. focus on one destination
    b. focus on one product
    c. 'a' and 'b'
    d. neither 'a' or 'b'
4. Liner shipping _____.
    a. Often uses containerization
    b. Has no defined port of call
    c. 'a' and 'b'
    d. None of the above
5. During the Canada-US Free Trade Agreement, _____ significantly increased employment in Canada.
    a. Canadian Tariff Cuts
    b. US Tariff Cuts
    c. US GDP Growth
    d. None of the above

Part 2: (10 points each)

1. Please list 3 pros and 3 cons of Ben and Jerry's expanding to international markets.

2. Please discuss three ways in which the Melitz firm-heterogeneity model differs from the standard trade model.

Part 3 – 10 Points each

Consider the "Melitz" exporting model we discussed in class. A firm must decide to exit the market or operate, and if the latter, whether to be purely domestic or a domestic firm that also exports. The returns from exiting are zero. If the firm decides to operate in some manner, it must pay F_0 in overhead costs. If the firm also decides to export, it must pay F_X in exporting fixed costs, such as up-front export financing. The firm can earn $\prod_H(\alpha)$ in the domestic market . If the firm exports, it earns $\prod_F(\alpha)$ in the foreign market, but loses 't' percent of these profits through a foreign tariff. The term α is firm level productivity, where each profit function is increasing in α.

1. Please graphically detail how firms sort into the three outcomes. Please comment on the relative productivity of each group of firms.

2. Suppose that due to a previous violation of international agreements, the foreign tariff 't' is reduced. However, in response, foreign increases "technical barriers to trade", such as red tape, product requirements, and other aspects that increase fixed exporting costs. Please detail graphically the *direct* effects of the change in tariffs and other costs. Can we say, with certainty, whether the group of exporting firms will expand or contract? If so, please detail this change. If not, briefly explain the intuition why not.

3. In problem 2 (of part 3), which group of firms is *always* more profitable after the change in policies. Please briefly discuss the intuition behind this result.