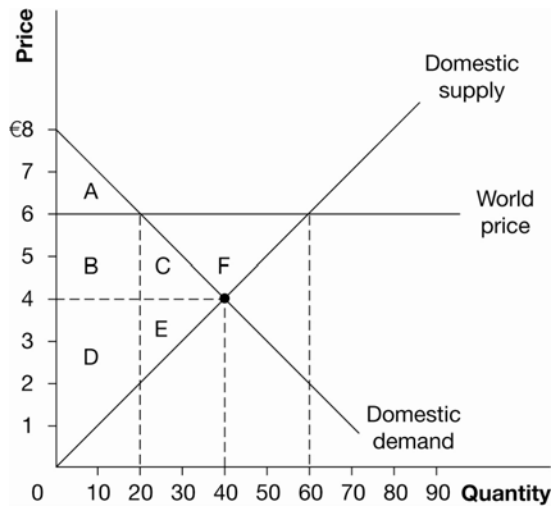


Chapter 9

1. Use Exhibit 3 to answer the following questions.

Exhibit 3



- a. If trade is not allowed, what is the equilibrium price and quantity in this market?

Answer:

Price = €4, quantity = 40 units.

- b. If trade is allowed, will this country import or export this commodity? Why?

Answer:

Export because the world price is above the domestic price which implies that this country has a comparative advantage in the production of this good.

- c. If trade is allowed, what is the price at which the good is sold, the domestic quantity supplied and demanded, and the quantity imported or exported?

Answer:

Price = €6, quantity supplied = 60 units, quantity demanded = 20 units, quantity exported = 40 units.

- d. What area corresponds to consumer surplus if no trade is allowed?

Answer:

A + B + C

- e. What area corresponds to consumer surplus if trade is allowed?

Answer:

A

f. What area corresponds to producer surplus if no trade is allowed?

Answer:

D + E

g. What area corresponds to producer surplus if trade is allowed?

Answer:

B + C + D + E + F

h. If free trade is allowed, who gains and who loses, the consumers or the producers, and what area corresponds to their gain or loss?

Answer:

Consumers lose B + C, producers gain B + C + F

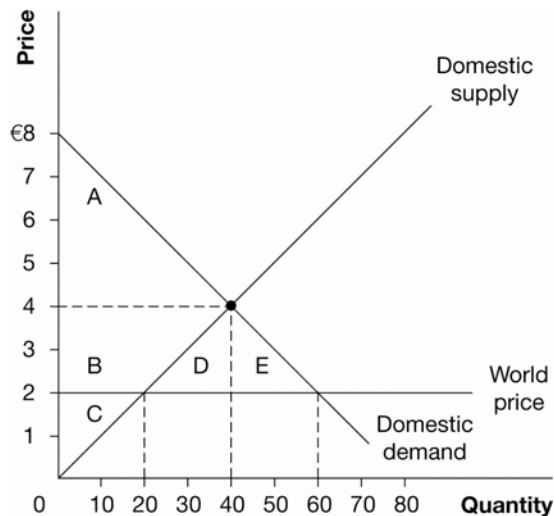
i. What area corresponds to the gains from trade?

Answer:

F

2. Use Exhibit 4 to answer the following questions.

Exhibit 4



a. If trade is not allowed, what is the equilibrium price and quantity in this market?

Answer:

Price = €4, quantity = 40 units.

b. If trade is allowed, will this country import or export this commodity? Why?

Answer:

Import because the world price is below the domestic price, which implies that other countries have a comparative advantage in the production of this good.

- c. If trade is allowed, what is the price at which the good is sold, the domestic quantity supplied and demanded, and the quantity imported or exported?

Answer:

Price = €2, quantity supplied = 20 units, quantity demanded = 60 units, quantity imported = 40 units.

- d. What area corresponds to consumer surplus if no trade is allowed?

Answer:

A

- e. What area corresponds to consumer surplus if trade is allowed?

Answer:

A + B + D + E

- f. What area corresponds to producer surplus if no trade is allowed?

Answer:

B + C

- g. What area corresponds to producer surplus if trade is allowed?

Answer:

C

- h. If free trade is allowed, who gains and who loses, the consumers or the producers, and what area corresponds to their gain or loss?

Answer:

Consumers gain B + D + E, producers lose B

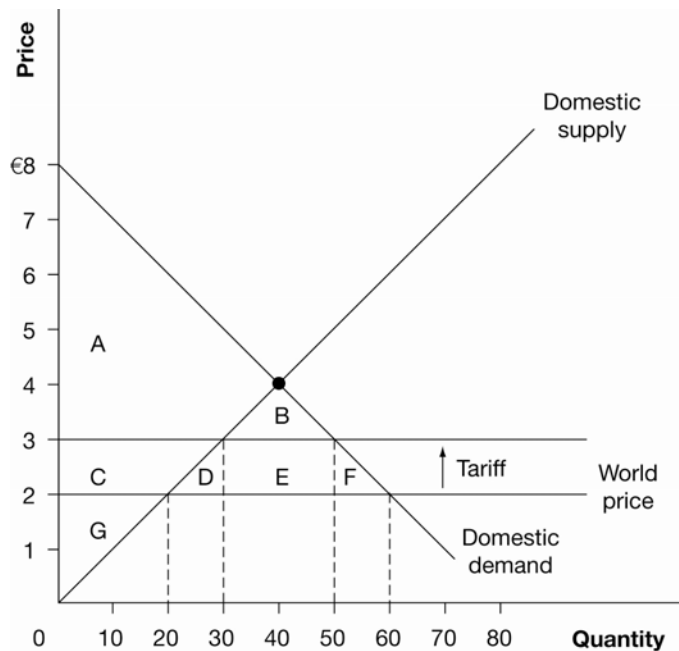
- i. What area corresponds to the gains from trade?

Answer:

D + E

3. Use Exhibit 5 to answer the following questions.

Exhibit 5



- a. If free trade is allowed, what is the domestic quantity supplied, domestic quantity demanded, and the quantity imported?

Answer:

Quantity supplied = 20 units, quantity demanded = 60 units, quantity imported = 40 units.

- b. If a €1 tariff is placed on this good, what is the domestic quantity supplied, domestic quantity demanded, and the quantity imported?

Answer:

Quantity supplied = 30 units, quantity demanded = 50 units, quantity imported = 20 units.

- c. What area corresponds to consumer and producer surplus before the tariff is applied?

Answer:

Consumer surplus = A + B + C + D + E + F, producer surplus = G

- d. What area corresponds to consumer surplus, producer surplus, and government revenue after the tariff is applied?

Answer:

Consumer surplus = A + B, producer surplus = C + G, government revenue = E

- e. What area corresponds to the deadweight loss associated with the tariff?

Answer:

D + F

- f. Describe in words the sources of the deadweight loss from a tariff.

Answer:

First, the rise in the price due to the tariff causes *overproduction* because units are produced that cost more than the world price. Second, the rise in price causes *underconsumption* because consumers fail to consume units where the value to consumers is greater than the world price.

- g. What is the size of the import quota that would generate results most similar to this €1 tariff?

Answer:

Import quota of 20 units—the same number of units imported with the €1 tariff.

- h. What is the size of the tariff that would eliminate trade altogether (i.e. that would return the market to its no-trade domestic solution)?

Answer:

A €2 tariff would raise the price to €4 (the no-trade domestic price) and eliminate trade.