

Course: International Trade and Policy

Week 4: Trade Theory II -- Beyond Comparative Advantage

Instructions: Please select the best answer for each of the following ten questions. Each question has only one correct answer.

Question 1

Which of the following is a critical puzzle that comparative advantage could NOT solve, leading to the need for "Beyond Comparative Advantage" models?

- A) The Gravity Model Puzzle
- B) The Leontief Paradox (1953)
- C) The Dixit-Stiglitz Paradox
- D) The Specific-Factors Equilibrium

Question 2

In the Specific-Factors model, what is the immediate short-run effect on labor allocation when the price of manufactured goods (P_M) rises due to trade?

- A) Labor moves from manufacturing to agriculture because wages rise faster in agriculture.
- B) Labor is immobile and cannot move between sectors.
- C) Labor moves from agriculture to manufacturing, driven by a higher value of the marginal product of labor (VMPL) in manufacturing.
- D) The nominal wage remains unchanged, so no labor moves.

Question 3

According to the Specific-Factors model, who are the unambiguous "winners" when a country opens to trade and the price of the exported manufactured good rises?

- A) Workers, because their nominal wage always rises more than the price increase.
- B) Landowners (specific to agriculture), because labor leaves the land.
- C) Owners of capital (specific to manufacturing), because the higher output price increases their real return.
- D) All factors of production benefit equally in the short run.

Question 4

What is the primary characteristic of "Internal Economies of Scale"?

- A) Cost advantages depend on the size of the entire industry cluster.
- B) A single firm's average cost decreases as its own output increases.
- C) Costs decrease due to geographic concentration of many small firms.
- D) Average cost remains constant regardless of the firm's output level.

Question 5

The Dixit-Stiglitz-Krugman model explains intra-industry trade between similar

countries by combining which two key elements?

- A) Constant returns to scale and perfect competition.
- B) Diminishing marginal returns and homogeneous products.
- C) Economies of scale (increasing returns) and consumer "love of variety."
- D) External economies and path dependence.

Question 6

What does the Grubel-Lloyd (GL) Index measure, and what does a GL value of 0.7 for US-Japan auto trade indicate?

- A) The level of inter-industry trade; a value of 0.7 indicates mostly inter-industry trade.
- B) The level of intra-industry trade; a value of 0.7 indicates a high degree of two-way trade in similar products (e.g., cars for cars).
- C) The impact of distance on trade; a value of 0.7 indicates a strong negative effect of distance.
- D) The degree of factor price equalization; a value of 0.7 indicates factor prices are 70% equalized.

Question 7

In the Gravity Model of trade, what do the "multilateral resistance terms" (Π_i , P_j) account for?

- A) The political resistance to signing free trade agreements.
- B) The average transportation cost within a single country.
- C) The fact that two countries trade more if they are both relatively isolated from the rest of the world.
- D) The effect of exchange rate volatility on trade flows.

Question 8

According to the lecture notes, what is a key policy implication derived from the Specific-Factors model?

- A) Free trade agreements need no complementary policies as all factors gain.
- B) Governments should use strategic subsidies to shift profits from foreign firms.
- C) Trade hurts some workers in the short run, so policy should include adjustment assistance (e.g., retraining and wage insurance).
- D) Regional trade agreements always increase welfare for all member countries.

Question 9

Which of the following is identified in the notes as a limitation of the "Beyond Comparative Advantage" models?

- A) They cannot explain any type of trade between similar countries.
- B) They assume that all factors of production are perfectly mobile between sectors.
- C) Increasing returns models often struggle to predict *which* product variety will win (multiple equilibria problem).
- D) They predict that trade never creates winners and losers within a country.

Question 10

In the Helpman-Krugman extensions, how do inter-industry and intra-industry trade coexist?

- A) Inter-industry trade is driven by economies of scale, while intra-industry trade is driven by factor endowments.
- B) Inter-industry trade (based on factor endowments) occurs for different goods, while intra-industry trade (based on variety) occurs within each sector.
- C) Inter-industry trade only happens between dissimilar countries, and intra-industry trade only happens in the long run.
- D) They cannot coexist; a country must specialize in one type of trade.

Answer Key

- 1. B
- 2. C
- 3. C
- 4. B
- 5. C
- 6. B
- 7. C
- 8. C
- 9. C
- 10. B