

Exam

Name _____

MULTIPLE CHOICE. Choose the one alternative that best completes the statement or answers the question.

- 1) What major dimension sets apart international finance from domestic finance? 1) _____
A) Foreign exchange and political risks B) Expanded opportunity set
C) Market imperfections D) all of the options

Answer: D

Topic: What's Special about "International" Finance?

- 2) An example of a political risk is 2) _____
A) adverse change in tax rules.
B) expropriation of assets.
C) the opposition party being elected.
D) both the expropriation of assets and adverse changes in tax rules are correct.

Answer: D

Topic: What's Special about "International" Finance?

- 3) Production of goods and services has become globalized to a large extent as a result of 3) _____
A) common tastes worldwide for the same goods and services.
B) natural resources being depleted in one country after another.
C) skilled labor being highly mobile.
D) multinational corporations' efforts to source inputs and locate production anywhere where costs are lower and profits higher.

Answer: D

Topic: What's Special about "International" Finance?

- 4) Recently, financial markets have become highly integrated. This development 4) _____
A) has increased the cost of capital for firms.
B) allows investors to diversify their portfolios internationally.
C) allows minority investors to buy and sell stocks.
D) none of the options

Answer: B

Topic: What's Special about "International" Finance?

- 5) Japan has experienced large trade surpluses. Japanese investors have responded to this by 5) _____
A) lobbying the Japanese government to allow the yen to appreciate.
B) liquidating their positions in stocks to buy dollar-denominated bonds.
C) investing heavily in U.S. and other foreign financial markets.
D) lobbying the U.S. government to depreciate its currency.

Answer: C

Topic: What's Special about "International" Finance?

- 6) Suppose your firm invests \$100,000 in a project in Italy. At the time the exchange rate is $\$1.25 = \text{€}1.00$. One year later the exchange rate is the same, but the Italian government has expropriated your firm's assets paying only $\text{€}80,000$ in compensation. This is an example of _____
- A) political risk.
 - B) market imperfections.
 - C) exchange rate risk.
 - D) none of the options, since $\$100,000 = \text{€}80,000 \times \$1.25/\text{€}1.00$.

Answer: A

Topic: What's Special about "International" Finance?

- 7) Suppose you start with \$100 and buy stock for £50 when the exchange rate is $\text{£}1 = \$2$. One year later, the stock rises to £60. You are happy with your 20 percent return on the stock, but when you sell the stock and exchange your £60 for dollars, you only get \$45 since the pound has fallen to $\text{£}1 = \$0.75$. This loss of value is an example of _____
- A) exchange rate risk.
 - B) weakness in the dollar.
 - C) political risk.
 - D) market imperfections.

Answer: A

Topic: What's Special about "International" Finance?

- 8) Suppose that Great Britain is a major export market for your firm, a U.S.-based MNC. If the British pound *depreciates* against the U.S. dollar, _____
- A) your firm will be able to charge more in dollar terms while keeping pound prices stable.
 - B) to protect U.K. market share, your firm may have to cut the dollar price of your goods to keep the pound price the same.
 - C) your firm may be priced out of the U.K. market, to the extent that your dollar costs stay constant and your pound prices will rise.
 - D) your firm may be priced out of the U.K. market, to the extent that your dollar costs stay constant and your pound prices will rise, and to protect U.K. market share, your firm may have to cut the dollar price of your goods to keep the pound price the same.

Answer: D

Topic: What's Special about "International" Finance?

- 9) Suppose Mexico is a major export market for your U.S.-based company and the Mexican peso appreciates drastically against the U.S. dollar. This means 9) _____
- A) your company's products can be priced out of the Mexican market, as the peso price of American imports will rise following the peso's fall.
 - B) your firm will be able to charge more in dollar terms while keeping peso prices stable.
 - C) your firm will be able to charge more in dollar terms while keeping peso prices stable and your domestic competitors will enjoy a period of facing lessened price competition from Mexican imports.
 - D) your domestic competitors will enjoy a period of facing lessened price competition from Mexican imports.

Answer: C

Topic: What's Special about "International" Finance?

- 10) Suppose Mexico is a major export market for your U.S.-based company and the Mexican peso depreciates drastically against the U.S. dollar, as it did in December 1994. This means that 10) _____
- A) your domestic competitors will enjoy a period of facing little price competition from Mexican imports.
 - B) your firm will be able to charge more in dollar terms while keeping peso prices stable.
 - C) your company's products can be priced out of the Mexican market, as the peso price of American imports will rise following the peso's fall.
 - D) none of the options

Answer: C

Topic: What's Special about "International" Finance?

- 11) Suppose that you are a U.S. producer of a commodity good competing with foreign producers. Your inputs of production are priced in dollars and you sell your output in dollars. If the U.S. currency depreciates against the currencies of our trading partners, 11) _____
- A) your competitive position is unchanged.
 - B) your competitive position is likely improved.
 - C) your competitive position is likely worsened.
 - D) none of the options

Answer: B

Topic: What's Special about "International" Finance?

- 12) Undoubtedly, we are now living in a world where all the major economic functions—consumption, production, and investment— 12) _____
- A) are still regional in nature.
 - B) are still inherently local.
 - C) are slowly becoming globalized.
 - D) are highly globalized.

Answer: D

Topic: What's Special about "International" Finance?

- 13) Most governments at least try to make it difficult for people to cross their borders illegally. This barrier to the free movement of labor is an example of 13) _____
- A) racial discrimination.
 - B) excessive transactions costs.
 - C) information asymmetry.
 - D) a market imperfection.

Answer: D

Topic: What's Special about "International" Finance?

- 14) Although the world economy is much more integrated today than was the case 10 or 20 years ago, a variety of barriers still hamper free movements of people, goods, services, and capital across national boundaries. These barriers include 14) _____
- A) information asymmetry.
 - B) excessive transportation costs.
 - C) legal restrictions.
 - D) all of the options

Answer: D

Topic: What's Special about "International" Finance?

- 15) The Japanese automobile company Honda decided to establish production facilities in Ohio, mainly to 15) _____
- A) reduce transactions costs.
 - B) reduce transportation costs.
 - C) circumvent trade barriers.
 - D) all of the options

Answer: C

Topic: What's Special about "International" Finance?

- 16) When individual investors become aware of overseas investment opportunities and are willing to diversify their portfolios internationally, 16) _____
- A) they should invest only in dollars or euros.
 - B) they should not bother to read or to understand the prospectus, since it's probably written in a foreign language.
 - C) they benefit from an expanded opportunity set.
 - D) they trade one market imperfection, information asymmetry, for another, exchange rate risk.

Answer: C

Topic: What's Special about "International" Finance?

- 17) The Nestlé Corporation, a well-known Swiss MNC, used to issue two different classes of common stock, bearer shares and registered shares, and foreigners were allowed to hold only 17) _____
- A) voting shares.
 - B) registered shares.
 - C) bearer shares.
 - D) convertible shares.

Answer: C

Topic: What's Special about "International" Finance?

- 18) Deregulated financial markets and heightened competition in financial services provided an environment for financial innovations that resulted in the introduction of various instruments. Examples of these innovative instruments include 18) _____
- A) international mutual funds, country funds, exchange traded funds.
 - B) currency futures and options, foreign stock index futures and options.
 - C) multicurrency bonds.
 - D) all of the options

Answer: D

Topic: What's Special about "International" Finance?

- 19) Nestlé, a well-known Swiss corporation, 19) _____
- A) at one time placed restrictions on foreign ownership of its stock. When it relaxed these restrictions, the total market value of the firm fell.
 - B) at one time placed restrictions on foreign ownership of its stock. When it relaxed these restrictions, there was a major transfer of wealth from foreign shareholders to domestic shareholders.
 - C) has been a paragon of virtue in its opposition to all forms of political risk.
 - D) none of the options

Answer: B

Topic: What's Special about "International" Finance?

- 20) The goal of shareholder wealth maximization 20) _____
- A) means that all business decisions and investments that a firm makes are done for the purpose of making the owners of the firm better off financially.
 - B) is a sub-objective the firm should attempt to achieve after the objective of customer satisfaction is met.
 - C) is not appropriate for non-U.S. business firms.
 - D) is in conflict with the privatization process taking place in third-world countries.

Answer: A

Topic: Goals for International Financial Management

- 21) As capital markets are becoming more integrated, the goal of shareholder wealth maximization 21) _____
- A) has been given increasing importance by managers in Europe.
 - B) has been altered to include other goals as well.
 - C) has been shown to be a deterrent to raising funds abroad.
 - D) has lost out to other goals, even in the U.S.

Answer: A

Topic: Goals for International Financial Management

- 22) Corporate scandals at firms such as Enron, WorldCom and the Italian firm Parmalat 22) _____
A) show that Italian shareholders are better at monitoring managerial behavior than U.S. shareholders.
B) show that socialism is a better way to go than capitalism.
C) show that white-collar criminals hardly ever get punished.
D) show that managers might be tempted to pursue their own private interests at the expense of shareholders.

Answer: D

Topic: Goals for International Financial Management

- 23) While the corporate governance problem is not confined to the United States, 23) _____
A) it has reached its high point in the United States.
B) the U.S. legal system, with lawsuits used only as a last resort, ensured that any conflicts of interest would soon be a thing of the past.
C) it can actually be a much more serious problem in other parts of the world, where the legal protection of shareholders is weak or nonexistent.
D) none of the options

Answer: C

Topic: Goals for International Financial Management

- 24) The owners of a business are the 24) _____
A) workers. B) suppliers. C) shareholders. D) taxpayers.

Answer: C

Topic: Goals for International Financial Management

- 25) The massive privatization that is currently taking place in developing and formerly socialist countries 25) _____
A) increases the opportunity set facing these countries' citizens.
B) depends on private investment.
C) will eventually enhance the standard of living to these countries' citizens.
D) all of the options

Answer: D

Topic: Goals for International Financial Management

- 26) A firm with *concentrated ownership* 26) _____
A) may enjoy more accounting transparency than firms with diffuse ownership structures.
B) is a partnership, never a corporation.
C) may give rise to conflicts of interest between dominant shareholders and small outside shareholders.
D) none of the options

Answer: C

Topic: Goals for International Financial Management

- 27) The *ultimate* guardians of shareholder interest in a corporation are the 27) _____
A) senior management. B) rank and file workers.
C) boards of directors. D) all of the options

Answer: C

Topic: Goals for International Financial Management

- 28) In countries like France and Germany, 28) _____
A) managers have traditionally embraced the maximization of shareholder wealth as the only worthy goal.
B) managers have often made business decisions with regard to maximizing market share to the exclusion of other goals.
C) managers have often regarded the prosperity and growth of their *combines*, or families of related firms, as their most critical goal.
D) managers have often viewed shareholders as one of the "stakeholders" of the firm, others being employees, customers, suppliers, banks and so forth.

Answer: D

Topic: Goals for International Financial Management

- 29) When corporate governance breaks down 29) _____
A) managers may be tempted to enrich themselves at shareholder expense.
B) shareholders are unlikely to receive fair returns on their investments.
C) the board of directors is not doing its job.
D) all of the options

Answer: D

Topic: Goals for International Financial Management

- 30) Privatization refers to the process of 30) _____
A) government allowing the operation of privately owned business.
B) prohibiting government operated enterprises.
C) a country divesting itself of the ownership and operation of a business venture by turning it over to the free market system.
D) having government operate businesses for the betterment of the public sector.

Answer: C

Topic: Globalization of the World Economy

- 31) Deregulation of world financial markets 31) _____
A) has encouraged developing countries such as Chile, Mexico, and Korea to liberalize by allowing foreigners to directly invest in their financial markets.
B) provided a natural environment for financial innovations, like currency futures and options.
C) has promoted competition among market participants.
D) all of the options

Answer: D

Topic: Globalization of the World Economy

- 32) The emergence of global financial markets is due in no small part to 32) _____
A) enforcement of the Soviet system of state ownership of resources of production.
B) government regulation and protection of infant industries.
C) advances in computer and telecommunications technology.
D) none of the options

Answer: C

Topic: Emergence of the Euro as a Global Currency

- 33) The common monetary policy for the euro zone is now formulated by 33) _____
A) the World Bank. B) the European Central Bank.
C) the Federal Reserve Bank. D) the Bundesbank in Germany.

Answer: B

Topic: Emergence of the Euro as a Global Currency

- 34) Since the end of World War I, the dominant global currency has been the 34) _____
A) British pound. B) U.S. dollar.
C) Japanese yen. D) Euro.

Answer: B

Topic: Emergence of the Euro as a Global Currency

- 35) Prior to World War I ending, the dominant global currency was the 35) _____
A) French franc. B) German mark.
C) British pound. D) Japanese yen.

Answer: C

Topic: Emergence of the Euro as a Global Currency

- 36) The ascendance of the dollar reflects several key factors, such as 36) _____
A) the mature and open capital markets of the U.S. economy.
B) the size of the U.S. population.
C) exchange rate stability.
D) all of the options

Answer: A

Topic: Emergence of the Euro as a Global Currency

- 37) The euro 37) _____
A) may eventually have a transaction domain larger than the U.S. dollar.
B) is divisible into 100 cents, just like the U.S. dollar.
C) is the common currency of Europe.
D) all of the options

Answer: D

Topic: Emergence of the Euro as a Global Currency

- 38) Since its inception the euro has brought about revolutionary changes in European finance. For example, 38) _____
- A) the European banking sector has become much more important as a source of financing for European firms.
 - B) Swiss bank accounts are all denominated in euro.
 - C) by redenominating corporate bonds and stocks from several different currencies into one common currency, the euro has precipitated the emergence of continent-wide capital markets in Europe that are comparable to U.S. markets in depth and liquidity.
 - D) there have actually not been any revolutionary changes.

Answer: C

Topic: Emergence of the Euro as a Global Currency

- 39) In David Ricardo's theory of comparative advantage, 39) _____
- A) international trade is a zero-sum game in which one trading partner's gain comes at the expense of another's loss.
 - B) liberalization of international trade will enhance the welfare of the world's citizens.
 - C) has been superseded by the now-orthodox view of mercantilism.
 - D) is a short-run argument, not a long-run argument.

Answer: B

Topic: Emergence of the Euro as a Global Currency

- 40) Under the theory of comparative advantage, liberalization of international trade will 40) _____
- A) enhance the welfare of the world's citizens.
 - B) result in higher prices in the long run as monopolist are able to charge higher prices after eliminating their competitors.
 - C) create unemployment and displacement of workers permanently.
 - D) all of the options

Answer: A

Topic: Emergence of the Euro as a Global Currency

- 41) Privatization is often seen as a cure for bureaucratic inefficiency and waste; some economists estimate that privatization improves efficiency and reduces operating costs by as much as 41) _____
- A) 15 percent. B) 5 percent. C) 10 percent. D) 20 percent.

Answer: D

Topic: Privatization

- 42) The World Trade Organization, WTO, 42) _____
- A) recently expelled China for human rights violations.
 - B) ruled that NAFTA is to be the model for world trade integration.
 - C) has the power to enforce the rules of international trade.
 - D) covers agriculture and physical goods, but not services or intellectual property rights.

Answer: C

Topic: Trade Liberalization and Economic Integration

- 43) Privatization 43) _____
- A) has allowed many governments to have the funds to nationalize important industries.
 - B) has guaranteed that new ownership will be limited to the local citizens.
 - C) has spurred a tremendous increase in cross-border investment.
 - D) has generally decreased the efficiency of the enterprise.

Answer: C

Topic: Privatization

- 44) The theory of comparative advantage 44) _____
- A) claims that no country has an absolute advantage over another country in the production of any good or service.
 - B) claims that economic well-being is enhanced if each country's citizens produce that which they have a comparative advantage in producing relative to the citizens of other countries, and then trade production.
 - C) claims that economic well-being is enhanced if each country's citizens produce only a single product.
 - D) claims that economic well-being is enhanced when all countries compare commodity prices after adjusting for exchange rate differences in order to standardize the prices charged all countries.

Answer: B

Topic: Trade Liberalization and Economic Integration

- 45) A multinational firm can be defined as a firm that 45) _____
- A) incorporated in one country and has production and sales operations in several other countries.
 - B) is incorporated in more than one country.
 - C) invests short-term cash inflows in more than one currency.
 - D) has sales affiliates in several countries.

Answer: A

Topic: Multinational Corporations

- 46) An MNC may gain from its global presence by 46) _____
A) pooling global purchasing power over suppliers.
B) utilizing their technological and managerial know-how globally with minimum additional costs.
C) spreading R&D expenditures and advertising costs over their global sales.
D) all of the options

Answer: D

Topic: Multinational Corporations

- 47) MNCs can use their global presence to 47) _____
A) boost profit margins and create shareholder value.
B) take advantage of underpriced labor services available in certain developing countries.
C) gain access to special R&D capabilities residing in advanced foreign countries.
D) all of the options

Answer: D

Topic: Multinational Corporations

- 48) Financial managers of MNCs should 48) _____
A) deal with (and take advantage of) market imperfections.
B) benefit from expanded investment and financing opportunities.
C) learn how to manage foreign exchange and political risks using proper tools and instruments.
D) all of the options

Answer: D

Topic: Multinational Corporations

- 49) A purely domestic firm that sources its products, sells its products, and raises its funds domestically 49) _____
A) can be more competitive than an MNC on its home turf due to superior knowledge of the local market.
B) can face stiff competition from a multinational corporation that can source its products in one country, sell them in several countries, and raise its funds in a third country.
C) can still face exchange rate risk, just like an MNC.
D) all of the options

Answer: D

Topic: Multinational Corporations

- 50) MNC stands for 50) _____
A) Multi-Nationalized Corporation. B) Multinational Corporation.
C) Military National Cooperation. D) none of the options

Answer: B

Topic: Multinational Corporations

- 51) Which is growing at a faster rate, foreign direct investment by MNCs or international trade? 51) _____
- A) International trade
 - B) FDI by MNCs
 - C) Since they are linked, they grow at the same rate.
 - D) none of the options
- Answer: B
Topic: Multinational Corporations
- 52) A true MNC, with operations in dozens of different countries 52) _____
- A) must effectively manage foreign exchange risk.
 - B) will pay taxes in only its home county.
 - C) can ignore foreign exchange risk since it is diversified.
 - D) none of the options
- Answer: A
Topic: Multinational Corporations
- 53) An MNC can 53) _____
- A) be a factor that increases the opportunity set of domestic investors.
 - B) increase economic efficiency.
 - C) be a factor that increases the opportunities of the citizens of less developed countries.
 - D) all of the options
- Answer: D
Topic: Multinational Corporations
- 54) Today for an MNC to produce merchandise in one country on capital equipment financed by funds raised in a number of different currencies through issuing securities to investors in many countries, and then selling the finished product to customers in yet other countries is 54) _____
- A) not uncommon.
 - B) extremely common.
 - C) the norm.
 - D) uncommon.
- Answer: A
Topic: Multinational Corporations
- 55) A corporation that can source its products in one country, sell them in another country, and raise the funds in a third country 55) _____
- A) enjoys a built-in hedge against political risk.
 - B) enjoys a built-in hedge against exchange rate risk.
 - C) is a domestic firm if all of the shareholders are from the same country.
 - D) is a multinational corporation.
- Answer: D
Topic: Multinational Corporations

56) Country A can produce 10 yards of textiles or 6 pounds of food per unit of input. Compute the opportunity cost of producing one additional unit of food instead of textiles. 56) _____

- A) 1.67 yards of textiles per pound of food
- B) 0.6 pounds of food per yard of textiles
- C) 0.6 yards of textiles per pound of food
- D) 1.67 pounds of food per yard of textiles

Answer: A

Topic: Appendix: The Theory of Comparative Advantage

57) The gains from trade 57) _____

- A) are likely realized in the long run when workers and firms have had the time to adjust to the new competitive environment.
- B) are smaller than the costs of adjustment.
- C) are immediately realized in the short run, when governments drop protectionist policies.
- D) none of the options

Answer: A

Topic: Appendix: The Theory of Comparative Advantage

58) Restrictions or impediments to free trade include such things as 58) _____

- A) import tariffs.
- B) costly transportation.
- C) import quotas.
- D) all of the options

Answer: D

Topic: Appendix: The Theory of Comparative Advantage

59) Suppose that country A is twice as good at producing widgets as country B. If the currency of B is twice as valuable as the currency of A, 59) _____

- A) the comparative advantage could be canceled out.
- B) trade will be an improved outcome for both A and B.
- C) the comparative advantage will shift to an absolute advantage.
- D) none of the options

Answer: A

Topic: Appendix: The Theory of Comparative Advantage

60) Comparative advantage 60) _____

- A) exists when one party can produce a good or service at a lower opportunity cost than another party.
- B) is also known as relative efficiency.
- C) can lead to trade even in the face of absolute efficiency.
- D) all of the options

Answer: D

Topic: Appendix: The Theory of Comparative Advantage

- 61) Country A can produce 10 yards of textiles or 6 pounds of food per unit of input. Country B can produce 8 yards of textiles or 5 pounds of food per unit of input. Which of the following statements is true? 61) _____
- A) Country A is relatively more efficient than Country B in the production of textiles.
 - B) Country A is relatively more efficient than Country B in the production of food.
 - C) Country B is relatively more efficient than Country A in the production of textiles.
 - D) none of the options

Answer: A

Topic: Appendix: The Theory of Comparative Advantage

- 62) Underlying the theory of comparative advantage are assumptions regarding 62) _____
- A) that the factors of production (land, labor, capital, and entrepreneurial ability) are relatively *immobile*.
 - B) that the factors of production (land, labor, capital, and entrepreneurial ability) are relatively mobile.
 - C) free trade between nations.
 - D) free trade between nations and that the factors of production (land, labor, capital, and entrepreneurial ability) are relatively *immobile*.

Answer: D

Topic: Appendix: The Theory of Comparative Advantage

- 63) If one country is twice the size of another country and is better at making almost everything than the benighted citizens of the smaller county, 63) _____
- A) the bigger county enjoys an absolute advantage.
 - B) the bigger county enjoys a comparative advantage.
 - C) the bigger county enjoys a relative advantage.
 - D) there is not enough information to make a determination.

Answer: A

Topic: Appendix: The Theory of Comparative Advantage

- 64) Country A can produce 10 yards of textiles or 6 pounds of food per unit of input. Country B can produce 8 yards of textiles or 5 pounds of food per unit of input. 64) _____
- A) Country A is relatively more efficient than Country B in the production of food.
 - B) Country B is relatively more efficient than Country A in the production of food, but Country A has an absolute advantage over Country B in the production of food and textiles.
 - C) Country A has an absolute advantage over Country B in the production of food and textiles.
 - D) Country B is relatively more efficient than Country A in the production of food.

Answer: B

Topic: Appendix: The Theory of Comparative Advantage

- 65) Country A can produce 10 yards of textiles or 6 pounds of food per unit of input. 65) _____
 Country B can produce 8 yards of textiles or 5 pounds of food per unit of input.
 A) Country B is relatively more efficient than Country A in the production of food.
 B) Country A is relatively more efficient than Country B in the production of textiles.
 C) Country A has an absolute advantage over Country B in the production of food and textiles.
 D) all of the options

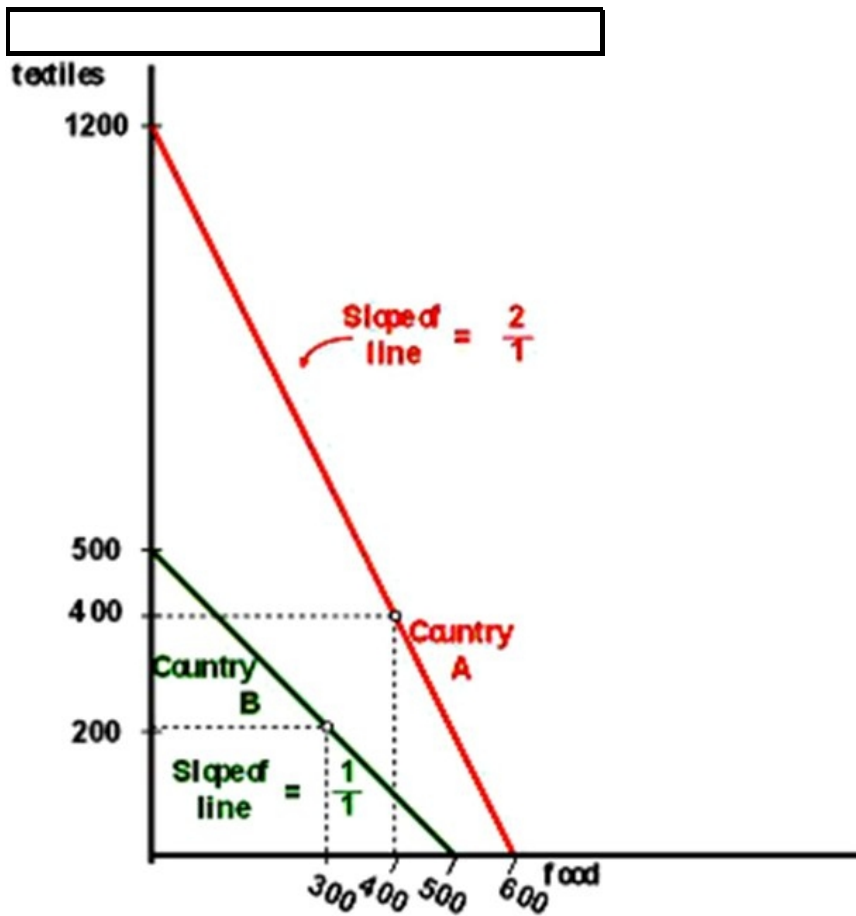
Answer: D

Topic: Appendix: The Theory of Comparative Advantage

- 66) Consider the no-trade input/output situation presented in the following table and graph for countries A and B. Assuming that free trade is legal; develop a scenario that will benefit the citizens of both countries. 66) _____

Input/Output without Trade

	Country		Total
	A	B	
I. Total Potential Output			
(lbs. or yard; 000,000s)			
Food	600	500	1,100
Textiles	1,200	500	1,700
II. Consumption			
(lbs. or yard; 000,000s)			
Food	300	400	700
Textiles	200	400	600



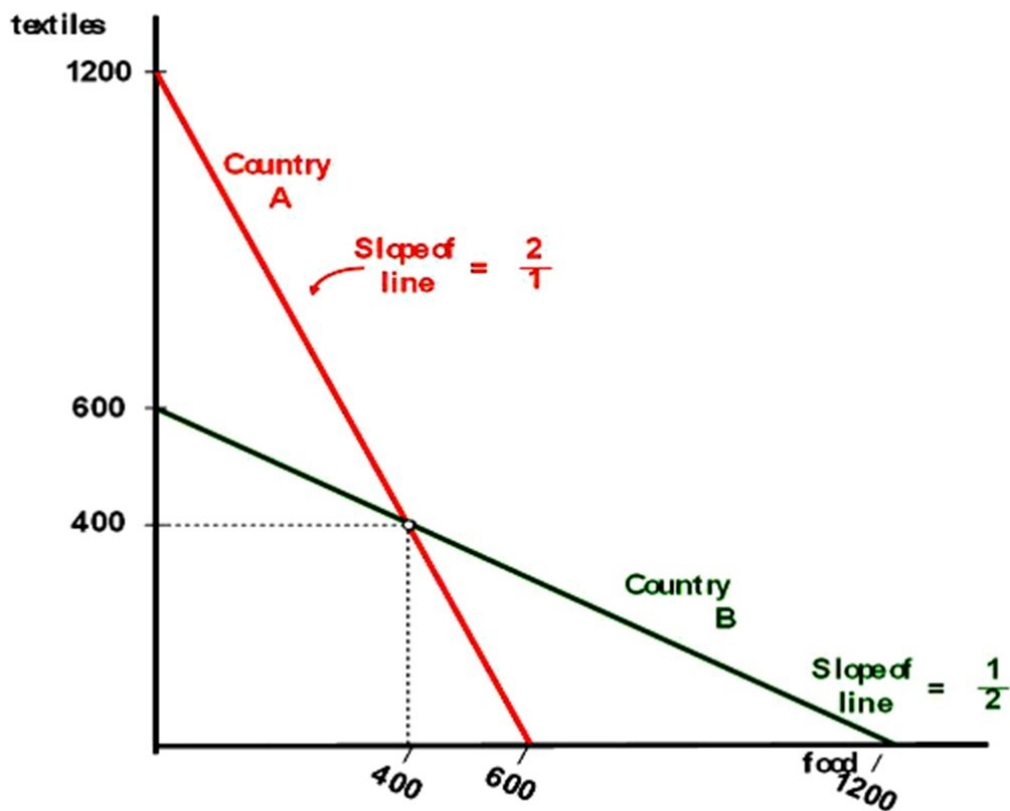
- A) Country B should make all the textiles and Country A should make all the food.
- B) Country A should make nothing but textiles and trade with Country B for food.
- C) Country B should make nothing but textiles and trade with Country A for food.
- D) Country B should make all the textiles and trade with Country A for food.

Answer: B

Topic: Appendix: The Theory of Comparative Advantage

67) Countries A and B currently consume 400 units of food and 400 units of textiles each and currently do not trade with one another. The citizens of country A have to give up one unit of food to gain two units of textiles, while the citizens of country B have to give up one unit of textiles to gain two units of food. Their production possibilities curves are shown.

67) _____



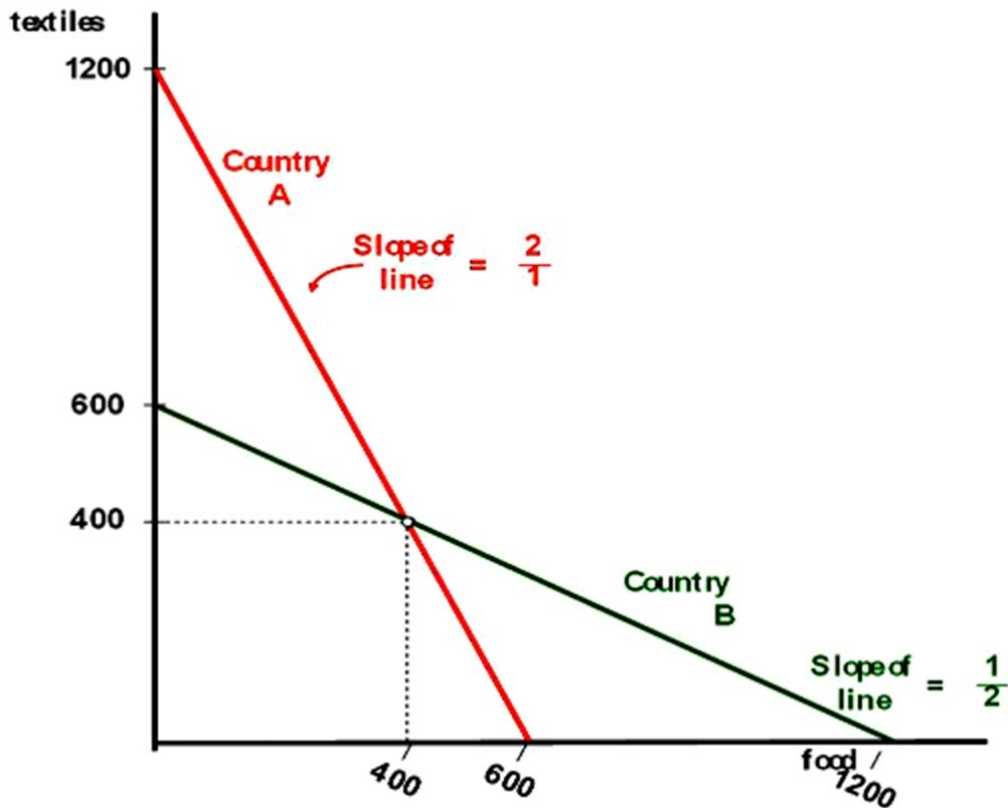
Under the theory of comparative advantage

- A) There are no gains from trade in this example.
- B) The citizens of country A should make textiles and trade with the citizens of country B for food.
- C) The citizens of country A should make food and trade with the citizens of country B for textiles.
- D) A is twice as good as B at making food and B is twice as good as A at making textiles.

Answer: B

Topic: Appendix: The Theory of Comparative Advantage

- 68) Counties A and B currently consume 400 units of food and 400 units of textiles each and currently do not trade with one another. The citizens of country A have to give up one unit of food to gain two units of textiles, while the citizens of country B have to give up one unit of textiles to gain two units of food. Their production possibilities curves are shown. 68) _____



Under the theory of comparative advantage, if free trade is allowed, the market clearing price (the exchange rate, if you will) between food and textiles will be

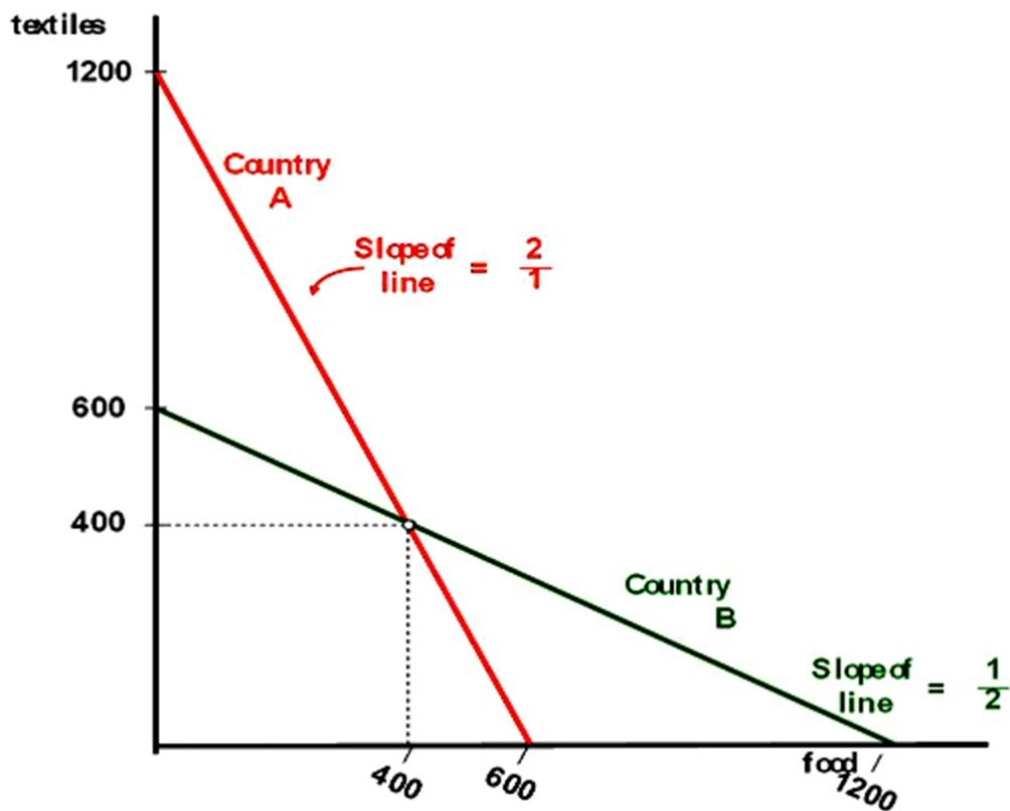
- A) two units of food for one unit of textiles.
- B) one unit of food for one unit of textiles.
- C) one unit of food for two units of textiles.
- D) somewhere between one unit of food for two units of textiles and two units of food for one unit of textiles.

Answer: D

Topic: Appendix: The Theory of Comparative Advantage

69) Countries A and B currently consume 400 units of food and 400 units of textiles each and currently do not trade with one another. The citizens of country A have to give up one unit of food to gain two units of textiles, while the citizens of country B have to give up one unit of textiles to gain two units of food. Their production possibilities curves are shown.

69) _____



Suppose that trade is allowed and that the international exchange rate between food and textiles is one-for-one. The increased consumption following trade will be

- A) an increase of 400 units of food and 400 units of textiles.
- B) an increase of 1,200 units of food and 1,200 units of textiles.
- C) there are no gains from trade in this example.
- D) an increase of 800 units of food and 800 units of textiles.

Answer: A

Topic: Appendix: The Theory of Comparative Advantage

70) In modern times, it is not a country per se but rather a controller of capital and know-how that gives the country in which it is domiciled a comparative advantage over another country. These controllers of capital and technology are

70) _____

- A) portfolio managers of international mutual funds.
- B) the multinational corporations (MNCs).
- C) the state.
- D) none of the options

Answer: B

Topic: Appendix: The Theory of Comparative Advantage

- 71) International trade is 71) _____
A) an "increasing-sum" game at which all players become winners.
B) a "zero-sum" game in which one country benefits at the expense of another country.
C) prone to both countries being worse off than had they not participated in international trade.
D) none of the options

Answer: A

Topic: Trade Liberalization and Economic Integration

- 72) The doctrine of comparative advantage was first put forth by 72) _____
A) David Ricardo. B) Adam Smith.
C) Ricky Ricardo. D) none of the options

Answer: A

Topic: Trade Liberalization and Economic Integration

- 73) The comparative advantage argument in free trade 73) _____
A) only works for two goods at a time. B) is a short-run argument.
C) ignores the cost of readjustment. D) none of the options

Answer: C

Topic: Appendix: The Theory of Comparative Advantage

- 74) If you can make a good product at a low *opportunity* cost, 74) _____
A) you should make something else that has a higher opportunity cost.
B) you would be well served to produce that good and trade for other goods.
C) you should make something else that has a higher value.
D) none of the options

Answer: B

Topic: Appendix: The Theory of Comparative Advantage

- 75) A country like North Korea 75) _____
A) engages in free trade.
B) likely rejects the notion of increased opportunity presented by free trade.
C) lies on a production possibilities curve superior to South Korea, since North Korea protects its international producers.
D) none of the options

Answer: B

Topic: Appendix: The Theory of Comparative Advantage

- 76) The table below shows the bushels of wheat and the bottles of beer that North and South Dakota can produce per day of labor under two different hypothetical situations (Cases I and II). 76) _____

	Case I		Case II	
	South Dakota	North Dakota	South Dakota	North Dakota
Wheat (bushels)	4	1	3	1
Beer (bottles)	1	2	4	2

Which state has an absolute advantage in producing wheat in Case I?

- A) South Dakota B) North Dakota C) Neither state D) Both states

Answer: A

Topic: Appendix: The Theory of Comparative Advantage

- 77) The table below shows the bushels of wheat and the bottles of beer that North and South Dakota can produce per day of labor under two different hypothetical situations (Cases I and II). 77) _____

	Case I		Case II	
	South Dakota	North Dakota	South Dakota	North Dakota
Wheat (bushels)	4	1	3	1
Beer (bottles)	1	2	4	2

Which state has an absolute advantage in producing beer in Case I?

- A) North Dakota B) South Dakota C) Neither state D) Both states

Answer: A

Topic: Appendix: The Theory of Comparative Advantage

- 78) The table below shows the bushels of wheat and the bottles of beer that North and South Dakota can produce per day of labor under two different hypothetical situations (Cases I and II). 78) _____

	Case I		Case II	
	South Dakota	North Dakota	South Dakota	North Dakota
Wheat (bushels)	4	1	3	1
Beer (bottles)	1	2	4	2

Which state has an absolute advantage in producing beer in Case II?

- A) South Dakota B) North Dakota C) Neither state D) Both states

Answer: A

Topic: Appendix: The Theory of Comparative Advantage

- 79) The table below shows the bushels of wheat and the bottles of beer that North and South Dakota can produce per day of labor under two different hypothetical situations (Cases I and II).

	Case I		Case II	
	South Dakota	North Dakota	South Dakota	North Dakota
Wheat (bushels)	4	1	3	1
Beer (bottles)	1	2	4	2

Which state has a comparative advantage in producing beer in Case I?

- A) North Dakota B) South Dakota C) Neither state D) Both states

Answer: A

Topic: Appendix: The Theory of Comparative Advantage

- 80) The table below shows the bushels of wheat and the bottles of beer that North and South Dakota can produce per day of labor under two different hypothetical situations (Cases I and II).

	Case I		Case II	
	South Dakota	North Dakota	South Dakota	North Dakota
Wheat (bushels)	4	1	3	1
Beer (bottles)	1	2	4	2

Which state has a comparative advantage in wheat production in Case I?

- A) South Dakota B) North Dakota C) Neither state D) Both states

Answer: A

Topic: Appendix: The Theory of Comparative Advantage

- 81) The table below shows the bushels of wheat and the bottles of beer that North and South Dakota can produce per day of labor under two different hypothetical situations (Cases I and II).

	Case I		Case II	
	South Dakota	North Dakota	South Dakota	North Dakota
Wheat (bushels)	4	1	3	1
Beer (bottles)	1	2	4	2

Which state has a comparative advantage in wheat production in Case II?

- A) North Dakota B) South Dakota C) Neither state D) Both states

Answer: B

Topic: Appendix: The Theory of Comparative Advantage

82) The table below shows the bushels of wheat and the bottles of beer that North and South Dakota can produce per day of labor under two different hypothetical situations (Cases I and II). 82) _____

	Case I		Case II	
	South Dakota	North Dakota	South Dakota	North Dakota
Wheat (bushels)	4	1	3	1
Beer (bottles)	1	2	4	2

What is the relative price of wheat in North Dakota prior to trade in Case II?

- A) 1 bushel of wheat = 2 bottles of beer
- B) 1 bushel of wheat = 1/2 bottle of beer
- C) 2 bushels of wheat = 1/2 bottle of beer
- D) 1/2 bushel of wheat = 2 bottles of beer

Answer: A

Topic: Appendix: The Theory of Comparative Advantage

83) The table below shows the bushels of wheat and the bottles of beer that North and South Dakota can produce per day of labor under two different hypothetical situations (Cases I and II). 83) _____

	Case I		Case II	
	South Dakota	North Dakota	South Dakota	North Dakota
Wheat (bushels)	4	1	3	1
Beer (bottles)	1	2	4	2

For case II, in what range must the "international" price of wheat fall? (*i.e.*, if North and South Dakota trade only with each other, what is the possible range of prices?)

- A) Between 1 bushel of wheat = 3/4 bottles of beer and 1 bushel of wheat = 1/2 bottles of beer
- B) Between 1 bushel of wheat = 3/4 bottles of beer and 1 bushel of wheat = 2 bottles of beer
- C) Between 1 bushel of wheat = 4/3 bottles of beer and 1 bushel of wheat = 2 bottles of beer
- D) none of the options

Answer: C

Topic: Appendix: The Theory of Comparative Advantage

84) For case II, let the international price be 1 bottle = 1 bushel. Derive South Dakota's "tradin 84) _____ possibilities curve."

	South Dakota			
	A	B	C	D
Wheat (bushels)	3	3	4	1
Beer (bottles)	4	3	4	2

- A) Option A B) Option B C) Option C D) Option D

Answer: C

Topic: Appendix: The Theory of Comparative Advantage

85) For case II, let the international price be 1 bottle = 1 bushel. Derive North Dakota's "tradin 85) _____ possibilities curve."

	South Dakota			
	A	B	C	D
Wheat (bushels)	2	3	1	2
Beer (bottles)	4	3	2	2

- A) Option A B) Option B C) Option C D) Option D

Answer: D

Topic: Appendix: The Theory of Comparative Advantage

86) The first two columns give the maximum daily amounts of beer and whiskey that Souther 86) _____ and Northern Ireland can produce when they completely specialize in one or another prod last two columns give each country's consumption without trade.

	Maximum beer production	Maximum whiskey production	Beer consumption without trade	Beer consumption without trade
Northern Ireland	500 kegs	1500 kegs	300 kegs	600 bottles
Southern Ireland	1200 kegs	800 kegs	600 kegs	400 bottles

What is the price of beer without trade in Southern Ireland?

- A) 2 bottles of whiskey = 3 kegs of beer
 B) 1 bottle of whiskey = 1 kegs of beer
 C) 5 bottles of whiskey = 12 kegs of beer
 D) none of the options

Answer: A

Topic: Appendix: The Theory of Comparative Advantage

87) The first two columns give the maximum daily amounts of beer and whiskey that Southern and Northern Ireland can produce when they completely specialize in one or another product. The last two columns give each country's consumption without trade.

	Maximum beer production	Maximum whiskey production	Beer consumption without trade	Whiskey consumption without trade
Northern Ireland	500 kegs	1500 kegs	300 kegs	600 bottles
Southern Ireland	1200 kegs	800 kegs	600 kegs	400 bottles

What is the price of beer without trade in Northern Ireland?

- A) 2 bottles of whiskey = 3 kegs of beer
- B) 2 bottles of whiskey = 1 keg of beer
- C) 5 bottles of whiskey = 12 kegs of beer
- D) none of the options

Answer: B

Topic: Appendix: The Theory of Comparative Advantage

88) The first two columns give the maximum daily amounts of beer and whiskey that Southern and Northern Ireland can produce when they completely specialize in one or another product. The last two columns give each country's consumption without trade.

	Maximum beer production	Maximum whiskey production	Beer consumption without trade	Whiskey consumption without trade
Northern Ireland	500 kegs	1500 kegs	300 kegs	600 bottles
Southern Ireland	1200 kegs	800 kegs	600 kegs	400 bottles

In which product does Northern Ireland have a comparative advantage in producing?

- A) Beer
- B) Whiskey
- C) Neither
- D) Both

Answer: B

Topic: Appendix: The Theory of Comparative Advantage

- 89) The first two columns give the maximum daily amounts of beer and whiskey that Southern and Northern Ireland can produce when they completely specialize in one or another product. The last two columns give each country's consumption without trade.

	Maximum beer production	Maximum whiskey production	Beer consumption without trade	Whiskey consumption without trade
Northern Ireland	500 kegs	1500 kegs	300 kegs	600 bottles
Southern Ireland	1200 kegs	800 kegs	600 kegs	400 bottles

Suppose that trade occurs. Each country completely specializes and 500 kegs of beer are traded for 500 bottles of whiskey. What is the international price of beer?

- A) 3 bottles of whiskey = 1 keg of beer B) 1 bottle of whiskey = 1 keg of beer
 C) 1 bottle of whiskey = 3 kegs of beer D) 2/3 bottle of whiskey = 1 keg of beer

Answer: B

Topic: Appendix: The Theory of Comparative Advantage

- 90) The first two columns give the maximum daily amounts of beer and whiskey that Southern and Northern Ireland can produce when they completely specialize in one or another product. The last two columns give each country's consumption without trade.

	Maximum beer production	Maximum whiskey production	Beer consumption without trade	Whiskey consumption without trade
Northern Ireland	500 kegs	1500 kegs	300 kegs	600 bottles
Southern Ireland	1200 kegs	800 kegs	600 kegs	400 bottles

What is the cost of Northern Ireland producing one additional bottle of whiskey?

- A) 3 kegs of beer B) 1 kegs of beer
 C) 0.33 kegs of beer D) 0.66 kegs of beer

Answer: C

Topic: Appendix: The Theory of Comparative Advantage

TRUE/FALSE. Write 'T' if the statement is true and 'F' if the statement is false.

- 91) The first two columns give the maximum daily amounts of beer and whiskey that Southern and Northern Ireland can produce when they completely specialize in one or another product. The last two columns give each country's consumption without trade. 91) _____

	Maximum beer production	Maximum whiskey production	Beer consumption without trade	Whiskey consumption without trade
Northern Ireland	500 kegs	1500 kegs	300 kegs	600 bottles
Southern Ireland	1200 kegs	800 kegs	600 kegs	400 bottles

Is Northern Ireland better off when it trades with Southern Ireland?

Answer: True False

Topic: Appendix: The Theory of Comparative Advantage

MULTIPLE CHOICE. Choose the one alternative that best completes the statement or answers the question.

- 92) The first two columns give the maximum daily amounts of beer and whiskey that Southern and Northern Ireland can produce when they completely specialize in one or another product. The last two columns give each country's consumption without trade. 92) _____

	Maximum beer production	Maximum whiskey production	Beer consumption without trade	Whiskey consumption without trade
Northern Ireland	500 kegs	1500 kegs	300 kegs	600 bottles
Southern Ireland	1200 kegs	800 kegs	600 kegs	400 bottles

What is the increased number of goods available in Northern Ireland after trade?

- A) 1,000 more bottles of whiskey and 500 more kegs of beer
- B) 400 more bottles of whiskey and 200 more kegs of beer
- C) 300 more bottles of whiskey and 300 more kegs of beer
- D) 200 more bottles of whiskey and 400 more kegs of beer

Answer: B

Topic: Appendix: The Theory of Comparative Advantage

93) Suppose that Northern Ireland and Southern Ireland each have 1,000 hours of labor per day. Southern workers are paid €1 per day and Northern workers are paid £1 per day. What is the *approximate* exchange rate associated with an international price of one keg of beer = 1 bottle of whiskey? 93) _____

A) €0.80 = £1

B) €1.14 = £1

C) €1 = £1

D) none of the options

Answer: B

Topic: Appendix: The Theory of Comparative Advantage

TRUE/FALSE. Write 'T' if the statement is true and 'F' if the statement is false.

94) Suppose that Northern Ireland and Southern Ireland each have 1,000 hours of labor per day. Southern workers are paid €1 per day and Northern workers are paid £1 per day. What is the *approximate* exchange rate associated with an international price of one keg of beer = 1 bottle of whiskey? 94) _____

Now suppose that Southern workers receive a raise to €2 per day. Will trade be possible at the exchange rate you found?

Answer: True False

Topic: Appendix: The Theory of Comparative Advantage

95) Suppose that Northern Ireland and Southern Ireland each have 1,000 hours of labor per day. Southern workers are paid €1 per day and Northern workers are paid £1 per day. What is the *approximate* exchange rate associated with an international price of one keg of beer = 1 bottle of whiskey? 95) _____

Now suppose that Southern workers are paid €1 per day but the Northern workers receive to £2 per day. Will trade be possible at the exchange rate you found?

Answer: True False

Topic: Appendix: The Theory of Comparative Advantage

MULTIPLE CHOICE. Choose the one alternative that best completes the statement or answers the question.

96) Consider a dentist and a 14-year old boy. The dentist can make \$100 per hour drilling teeth and the 14-year old boy can make \$2 per hour picking up used aluminum cans. The dentist is a manly man and can mow his half-acre lot in one hour. The 14-year old boy can mow the lawn in two hours. If the dentist hires the boy to mow his lawn at any price less than \$100, but more than \$4 96) _____

A) the dentist would be exploiting the boy.

B) the boy would be exploiting the dentist.

C) both he and the boy are better off.

D) all of the options

Answer: C

Topic: Appendix: The Theory of Comparative Advantage

97) Consider the no-trade input/output situation presented in the following table and graph for _____ and North Carolina. Assume that free trade is legal.

Input/Output without Trade

	Country		
	South Carolina	North Carolina	Total
I. Total Potential Output			
(lbs. or yards; 000,000s)			
Guns	500	250	750
Butter	1,000	750	1,750
II. Consumption			
(lbs. or yards; 000,000s)			
Guns	250	200	450
Butter	500	150	650

Which state is better at making guns?

- A) North Carolina
- B) South Carolina
- C) The states are equally good at making guns.

Answer: B

Topic: Appendix: The Theory of Comparative Advantage

98) Consider the no-trade input/output situation presented in the following table and graph for _____ and North Carolina. Assume that free trade is legal.

Input/Output without Trade

	Country		
	South Carolina	North Carolina	Total
I. Total Potential Output			
(lbs. or yards; 000,000s)			
Guns	500	250	750
Butter	1,000	750	1,750
II. Consumption			
(lbs. or yards; 000,000s)			
Guns	250	200	450
Butter	500	150	650

How much does it cost for North Carolina to produce one gun?

- A) 1.33 pounds of butter
- B) .33 pounds of butter
- C) 3 pounds of butter
- D) none of the options

Answer: C

Topic: Appendix: The Theory of Comparative Advantage

99) Consider the no-trade input/output situation presented in the following table and graph for South Carolina and North Carolina. Assume that free trade is legal.

Input/Output without Trade

	Country		
	South Carolina	North Carolina	Total
I. Total Potential Output			
(lbs. or yards; 000,000s)			
Guns	500	250	750
Butter	1,000	750	1,750
II. Consumption			
(lbs. or yards; 000,000s)			
Guns	250	200	450
Butter	500	150	650

What is the relative price of a gun in terms of butter in South Carolina?

- A) 2 guns cost 1 pounds of butter.
- B) 1 gun costs 3 pounds of butter.
- C) 1 gun costs 2 pounds of butter.
- D) 3 guns cost 1 pounds of butter.

Answer: C

Topic: Appendix: The Theory of Comparative Advantage

100) Consider the no-trade input/output situation presented in the following table and graph for South Carolina and North Carolina. Assume that free trade is legal.

Input/Output without Trade

	Country		
	South Carolina	North Carolina	Total
I. Total Potential Output			
(lbs. or yards; 000,000s)			
Guns	500	250	750
Butter	1,000	750	1,750
II. Consumption			
(lbs. or yards; 000,000s)			
Guns	250	200	450
Butter	500	150	650

What is the relative price of a pound of butter in terms of guns in North Carolina?

- A) 1 pound of butter costs 0.66 guns.
- B) 1 pound of butter costs 0.33 guns.
- C) 2 guns costs 0.66 pounds of butter.
- D) 1 gun costs 0.33 pounds of butter.

Answer: B

Topic: Appendix: The Theory of Comparative Advantage