Homework 1
Due in class, Thursday March 3

This is worth 10% of total grade for the course

Guidelines: By all means work with others in thinking about solutions, but please make sure that you turn in only your own work. When drawing diagrams, be sure to label all relevant curves and points.

1. Protectionism (tariffs on imported goods) was a popular way of getting industrialization started in Southeast Asia. Use the 4-quadrant diagram of an economy producing two goods, agriculture (A) and manufacturing (M) to answer the following questions.

a. Show an initial equilibrium under assumed free trade, so that the domestic relative price of M to A reflects the world price ratio.

b. On the same diagram, show the effect of a tariff that raises the domestic price of manufactures while leaving agricultural prices unchanged. Show the differences from the free trade equilibrium on production, and on employment in each sector.

c. Using the constant (initial) price ratio of manufactures to agricultural goods, show the effect of the tariff on GDP, measured in terms of manufactures. Does national income rise or fall when the tariff is applied?

2. What do you think the tariff in question 1 will do the real wage earned by workers in this economy? What about the real earnings of owners of capital used in manufacturing and land used in agriculture? Explain in 1-2 sentences.